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Minutes of Executive Board Meeting 15/9-1

10:00 a.m., January 28, 2015

1. Islamic Republic of Mauritania—2014 Article IV Consultation

Documents: SM/15/5 and Correction 1; SM/15/6 and Correction 1, and Correction 2, and Supplement 1, and Supplement 1, Correction 1, and Supplement 2, and Supplement 3; SM/15/8

Staff: Vera Martin, MCD; Oliva, MCM; Ghura, SPR

Length: 31 minutes

Executive Board Attendance

N. Shinohara, Acting Chair

Executive Directors	Alternate Executive Directors
	M. Mkwezalamba (AE)
	M. Raghani (AF)
	V. De la Barra (AG), Temporary
	K. Moon (AP), Temporary
	R. Espinel (BR), Temporary
	X. Li (CC), Temporary
	J. Cova (CE), Temporary
	T. Lessard (CO), Temporary
I. Çanakci (EC)	
	T. Guyon (FF)
	A. Landbeck (GR), Temporary
	M. Govil (IN), Temporary
	I. Lopes (IT), Temporary
	K. Masuhara (JA), Temporary
	M. Daïri (MD)
H. Beblawi (MI)	
	V. Volociuc (NE), Temporary
	M. Lindpere (NO), Temporary
	D. Vasilyev (RU), Temporary
F. Alshathri (SA)	
	T. Marcelo (ST), Temporary
	I. Rajabov (SZ), Temporary
	D. Hall (US), Temporary
	P. Stevens (UK), Temporary

A. Zanello, Acting Secretary
R. Dall'Orto, Summing Up Officer
L. Briamonte, Board Operations Officer
P. Martin, Verbatim Reporting Officer

Also Present
Communications Department: R. Elnagar. Finance Department: A. Alsadig. Legal Department: K. Christopherson Puh, G. Otokwala. Middle East and Central Asia Department: M. Ahmed, A. Toure, M. Vera Martin. Monetary and Capital Markets Department: C. Baba, R. Cervantes, M. Oliva. Strategy, Policy, and Review Department: D. Ghura, F. Ricka. Alternate Executive Director: W. Diallo (AF), W. Kiekens (NE). Senior Advisors to Executive Directors: S. Bah (AF), A. Ismael (AF), G. Letilly (FF), M. Sidi Bouna (AF). Advisors to Executive Directors: K. Badsi (MD), R. Kharel (ST), M. Matsutani (JA), M. Merhi (MI), B. Repansek (EC).

1. ISLAMIC REPUBLIC OF MAURITANIA—2014 ARTICLE IV CONSULTATION

Mr. Yambaye and Mr. Sidi Bouna submitted the following statement:

Introduction

Mauritania has made significant progress in recent years towards both raising economic growth and achieving macroeconomic stability. Real GDP growth averaged over 5 percent in the past decade owing to the exploitation of the country’s large fishing and mineral resources, most notably iron ore but also copper and gold. Fiscal revenues rose significantly, and sound macroeconomic management along with the mining sector’s rapid expansion has enabled the buildup of sizable external and fiscal buffers. While prudent policies and a favorable external environment have played a key role, my authorities also recognize and appreciate the support and candid policy advice of staff and the Fund, over the years, in this improved performance.

Mauritania also made some progress in the area of poverty reduction, including through improved targeting of social safety nets and investment in key social projects to address the country’s immense infrastructure gap. They acknowledge, however, that much remains to be done in this area. In particular, as noted in the report, progress towards the MDGs has been mixed. They would like nonetheless to reiterate that the fight against poverty remains at the center of their development agenda and that they will continue to promote growth-enhancing polices that are also inclusive in nature, in order to address the population’s large social needs and provide employment opportunities, especially for the youth. They are aware that reaching their ambitious objectives in this area requires continued improvement in the country’s business climate and renewed efforts to accelerate the development of the private sector.

Given the importance of natural resources in Mauritania’s economy, its recent performance and the economic outlook has been adversely affected by the steep decline in the international prices of the main commodities exported and the economic slowdown in key trading partners. These external developments constitute the key downside risk to the Mauritania’s outlook. However, my authorities expect that the country’s external buffers built in recent years and the lower international oil and food prices (Mauritania being a net importer of both) will help mitigate the impact of external shocks. Going forward, they view as their key short-term challenge, the implementation of well-designed policies to address these external risks, while preserving the hard-won macroeconomic gains, as buffers are being increasingly used.

Negotiations on the EU fishing compensation are ongoing and my authorities expect an agreement that will be mutually beneficial to all parties.

Over the longer term, the focus as rightly underscored by staff will be to enhance the economy's resilience to shocks, including through the imperative diversification of the economy away from natural resources. My authorities share the overall assessment by staff along with the key identified challenges which they intend to address in close coordination with the Fund and other key partners.

Recent Economic Developments and Outlook

Growth: While real GDP growth is projected to slow down slightly to 5.5 percent in 2015, from 6.4 percent in 2014, the external and fiscal sectors will be the most affected by the decline in the international prices of iron ore, copper, and gold exported by Mauritania.

External sector: The substantial deterioration in the terms of trade and large FDI-related imports are having a significant adverse impact on the trade and current account balances, and on the level of foreign exchange reserves (dropping from 6.6 months of imports cover in 2013 to 4.7 months in 2014) despite the favorable effect of lower international oil and food prices.

Fiscal sector: The fiscal deficit is estimated to have widened to 3.9 percent of GDP in 2014, from 1.7 percent in 2013, despite the decline in both current and capital expenditures. This is due in part to the drop in the contribution of SNIM (the national iron ore mining company) and other mining companies to the budget.

Inflation: It remains in check and is expected to stay moderate over the medium term (within the approximate 4-5 percent range) thanks to lower international food and fuel prices, and a prudent monetary policy stance.

Outlook: In spite of the fall in iron ore prices and slower economic activity, the short- and medium-term outlook remains broadly favorable. Real GDP over the medium-term is expected to average over 6 percent reflecting in part increased mining activity coming from new mines. The fiscal deficit is projected to narrow gradually from 1.9 percent of non-extractive GDP in 2015 to 1.3 percent by 2013. The buildup of international reserves is projected to resume in 2015 to reach 6.5 months of imports cover by 2019.

Policy Adjustments to External Risks

While the outlook remains favorable, the economy faces important risks in the near to medium term, and my authorities will continue to work closely with staff to design and implement the necessary policies that will help preserve macroeconomic stability and continued economic growth.

Fiscal policy adjustments: My authorities are addressing the projected decline in revenues from the mining sector in the 2015 budget through an increase in the VAT rate (from 14 to 16 percent) and cuts in current expenditures, while containing the increase in the public sector wages within a level that does not increase the ratio of the wage bill as a percentage of non-extractive GDP. The wage bill is actually projected to decline to 8.3 percent of non-extractive GDP in 2015, from 8.4 percent in 2014 and 9 percent in 2013.

As a medium- to long-term fiscal policy reform, my authorities very much welcomed the discussion on a fiscal rule in a country like Mauritania with relatively abundant mineral resources. However, they would like to emphasize that on the issue of pro-cyclicality of fiscal policy, it is important to note, first, that while spending had increased during the recent mining sector boom, budget revenues from non-extractive industries as a share of GDP have also increased substantially, as my authorities continued to broaden the tax base and strengthen fiscal revenue administration. Second, and more importantly, my authorities believe that the implementation of a fiscal rule in a low-income country like Mauritania with considerable basic social infrastructure needs would inevitably delay the implementation of their development agenda and ultimately weigh on the ongoing policy efforts to accelerate the fight against poverty. Therefore, in the short-term, they believe that the focus should remain on implementing projects that are deemed viable and that take into account the country's absorptive capacity constraints. Nonetheless, they look forward to continued constructive discussions with staff on this issue, as a potential and significant long-term reform.

Monetary policy and exchange rate policy adjustments: My authorities agree with staff that with declining foreign exchange reserves, now is a right time to strengthen the monetary policy framework and reestablish the use of more direct and traditional liquidity management instruments such as interest rates and reserve requirements, and limit the use of indirect instruments like foreign exchange interventions and treasury bills. They look forward to continue discussions with staff on the formalization of monetary policy and the liquidity management framework. My authorities also agree that in the context of declining reserves, a more flexible exchange rate would contribute to acting as shock absorber. They are of the view, however, that given Mauritania's very shallow foreign exchange market, characterized by considerably higher demand over supply, the liberalization of the foreign exchange market should remain gradual.

My authorities welcome the assessment of Mauritania's financial sector stability and thank staff for the findings and recommendations made in the FSSA report. They would like to reiterate their commitment to implementing the recommendations made in the report, as rapidly as possible, and according to the agreed timeframe.

Other Issues

Deterioration of the risk of debt distress: Mauritania's public sector debt has risen to an estimated 78.4 of GDP in 2014 (from 73.7 percent in 2013). The downward revision of the country's risk of debt distress (from moderate to high) is a concern to my authorities, especially given that this revision is taking place at a time when they are facing daunting external challenges which are having an immediate and direct impact on the economy. They remain committed however to a prudent external borrowing policy and look forward to further discussions with the IMF and the World Bank on improving the institutional environment and stabilizing debt levels, including in the context of the new public debt limits policy framework.

Obligations under Article VIII: My authorities take note of the report's findings and will continue to address the remaining restrictions highlighted in the report, with a view to meeting all obligations under Article VIII. In the meantime, they request the Board's approval to temporarily maintain the remaining exchange restriction which, as indicated by staff, is necessary for balance of payments reasons and does not discriminate among IMF members. As also indicated in the report, my authorities will eliminate the remaining restrictions within one year.

Conclusion

Mauritania has made important progress in the past few years in improving economic and financial performance, and raising economic growth. However, the economy faces important challenges in the foreseeable future resulting from increased external risks which have exposed the economy's vulnerability to terms of trade shocks and could jeopardize the recent hard-won macroeconomic stability gains. In this regard, my authorities will continue to work closely with staff to put in place the necessary policies to address the risks, preserve the gains achieved and also continue their efforts to develop the economy. In this endeavor, they will work closely with the Fund staff and their development partners.

Mr. Haarsager and Mr. Hall submitted the following statement:

Building on reforms undertaken in its previous ECF and supported by a commodity-driven boom, Mauritania has achieved strong growth and macroeconomic stability in recent years. Policy buffers built up over this period are now being tested by the recent sharp decline in commodity prices and slowdowns in key export markets, including Europe and China. With near-term risks tilted notably to the downside, managing the challenges ahead will require a prudent fiscal framework, stronger structural reform efforts to promote economic diversification, enhanced exchange rate flexibility to facilitate adjustment, and reforms to promote financial stability.

Despite fiscal reforms that have delivered substantial improvements in revenue collection, external debt (including public and publicly guaranteed debt) has continued to rise. Given the staff's assessment that Mauritania, a post-HIPC country, is at high risk of debt distress, and that it is vulnerable to deteriorating terms of trade (as seen recently), we would stress the importance of a stronger fiscal framework. We welcome the staff's calls for a medium-term expenditure framework to direct and monitor fiscal policy, particularly capital investment, and for establishment of a fiscal stabilization fund that would help manage resource-related revenue volatility. We would also stress action to improve the composition of expenditure, as shifting from broad-based subsidies to better-targeted cash transfers can rationalize expenditures while enhancing social protection. Can the staff comment on the prospects for formal adoption of the Organic Budget Law, which has awaited approval since 2012?

Mauritania's continued ability to attract significant FDI, and the current plans for substantial export-related investments through 2019, should be supportive of medium-term growth. Nonetheless, the current account deficit remains substantial, even when excluding FDI-financed imports related to extractive industries, and will be further pressured if terms of trade continue deteriorating. Further, the projected strengthening of the balance of payments beyond 2020 relies on rapid production and export growth on a narrow resource base, leaving Mauritania exposed to external shocks. This underscores the importance of bolstering external buffers and rebuilding reserve coverage. Increasing exchange rate flexibility would create an additional channel to facilitate adjustment. In this regard, we are pleased with the progress authorities have made in eliminating multiple exchange rates, and urge expeditious elimination of remaining foreign exchange restrictions.

External vulnerability would also be reduced by stronger efforts to promote economic diversification. As highlighted in the useful selected issues paper, average productivity growth has been negative for more than a decade, emphasizing the need for structural reforms. Improvements to education and other human capital investments would promote more inclusive growth and allow Mauritania to capitalize on its coming demographic dividend. With Mauritania comparing poorly to neighbors in the ease of doing business and quality of infrastructure, stronger efforts are needed to improve the institutional environment, reduce administrative burdens, simplify regulations, and scale up infrastructure investment. An improved business environment should facilitate investment in non-resource sectors and diversify growth.

Financial sector reforms would allow for greater extension of credit and diversification of investment while preserving financial stability. The Financial System Stability Assessment lays out an appropriately ambitious reform agenda. We would highlight extending central bank supervision to include the national development bank and the insurance sector, strengthening supervisory independence, and creating a robust independent resolution authority. Can the staff comment on the trade-offs that might be involved in their suggestion that the national development bank might serve as a primary bank to promote long-term credit, such as the benefits of longer-term funding for banks against the risk that this could inhibit the development of private funding markets?

Mr. Snel and Ms. Volociuc submitted the following statement:

We thank staff for an insightful set of reports and Messrs. Yambaye and Sidi for their informative buff statement. The Mauritanian authorities have made good progress by pursuing an appropriate policy mix under the ECF program during 2010-2013. Nonetheless, as staff points out in the Article IV consultations report, significant challenges remain in the medium term. Risks are tilted to the downside mostly due to lower iron ore prices. We encourage the authorities to carry on their efforts to maintain a prudent macroeconomic policy, preserve fiscal sustainability, safeguard financial stability and encourage private sector development. We broadly share the thrust of the staff appraisal and wish to limit our comments to the following points for emphasis.

We commend the authorities for the marked progress achieved with their fiscal policy formulation in the past, but important challenges ahead highlight the need to address complex fiscal policy objectives. The ECF arrangement paved the way for a more prudent fiscal stance and we welcome the authorities' commitment to maintain a prudent fiscal policy. Although the favorable macroeconomic outlook will support fiscal consolidation efforts over the medium term, we support staff's view on the need to ensure long-run fiscal sustainability, manage resource revenue uncertainty and volatility through precautionary financial buffers. A step forward would be to make progress with the initiated reforms on public financial management envisaging fiscal principles, objectives and the medium term expenditure framework. How appropriate is the implementation of a fiscal rule in Mauritania given the current conditions? Enhancing debt management along with ensuring prudent external borrowing is crucial given the high risk of debt distress.

Reforming the banking sector aimed at achieving a more robust financial system would contribute to restoring confidence in the sector. While the staff report shows that the banks are broadly well capitalized and liquid, the banking sector remains vulnerable to shocks. The low financial penetration rates as well as weak financial inclusion limit the banking activity to short-term loans. Weak banking supervision and regulatory enforcement make the system more vulnerable to a loss of confidence. Furthermore, important deficiencies remain in the AML/CFT framework. We urge the authorities to take full advantage of the recent FSSA's detailed analysis and initiate the needed reforms to further strengthen the financial sector, facilitate long-term credit to the private sector and encourage financial deepening and inclusion as well as to set up a macroprudential policy and crisis management framework. Could staff elaborate on the implementation capacity of the FSAP recommendations?

The focus of the monetary authorities should be on ensuring the operational independence and accountability of the central bank. The monetary framework needs to be strengthened by developing liquidity management forecasts, expanding monetary instruments, increasing the role of the exchange rate as a shock absorber and strengthening governance and institutional capacity for the conduct of monetary policy. We also support staff's advice to improve the effectiveness of the central bank as well as reviewing its legal framework in order to allow the bank to pursue an adequate monetary policy, including the recapitalization of the central bank.

Steady implementation of structural reforms is critical to boost potential growth and further reduce poverty. Particularly important are the improvement of the business environment, physical infrastructure, human resources development and the governance framework. A more dynamic private sector will be critical to diversify the economy, create jobs and reduce poverty, as well as to ensure a sustained and inclusive growth.

Mr. Beblawi and Ms. Merhi submitted the following statement:

Economic growth in Mauritania has been high, mostly driven by infrastructure investment, mining production and services. Medium-term growth prospects remain favorable, with the country expected to be one of the best performers in the region. However, the economy faces important challenges arising from the steep decline in the price of exported commodities as well as the economic slowdown in key trading partners. The country’s external buffers which were built in recent years and the lower international oil prices will help mitigate the impact of external shocks, as noted by Messrs. Yambaye and Sidi Bouna, in their helpful buff. We concur with the staff’s assessment and would like to highlight the following issues:

The authorities’ commitment to fiscal consolidation is essential to maintain fiscal sustainability. Despite progress in revenue mobilization and expenditure discipline, external debt remains elevated, and we take note of the deterioration of the risk of debt distress. The budget’s high dependence on volatile mining revenues poses challenges to fiscal management especially given the declining prices in global commodity markets and particularly in iron ore, which represent half of the country’s exports. We concur with staff that whether this term-of trade shock is temporary or sustained, effective management of natural resources is needed and will require a well-adapted macro-fiscal framework. We note in this regard that the authorities consider that the introduction of fiscal rules is premature at this stage. We welcome the measures taken in the 2015 budget—namely the increase in VAT by two percentage points and cuts in current expenditures—to offset the decline in mining revenues. The protection of social spending and the introduction of a well targeted social safety net should remain a priority, especially given the high poverty rates.

We concur with staff that Mauritania need to build external buffers to support external stability and liberalize the foreign exchange market. Indeed, and in a context of declining reserves, a more flexible exchange rate would contribute to acting as shock absorber. However, we can sympathize with the authorities’ views that the liberalization of the foreign exchange market should remain gradual, given Mauritania’s very shallow foreign exchange market. Strengthening the monetary policy framework and enlarging the set of liquidity management tools will improve the transmission mechanism to the economy and help manage liquidity more effectively.

The banking system is well capitalized and liquid but remains susceptible to shocks, as noted in the Financial System Stability Assessment. Asset quality remains weak with non-performing loans (NPLs) around 20 percent, provisioning is also weak in some banks and profitability is low. We would appreciate more elaboration from staff on what measures are being considered to address the high level of NPLs, as well as the issue of the under-provisioning of some banks. The authorities have taken steps to strengthen supervision and the regulatory framework, but more efforts are needed on the enforcement side, in addition to enhancing the bank resolution regime and introducing early warning solvency and liquidity indicators.

While Mauritania has succeeded in restoring macroeconomic stability, further efforts are needed to tackle the high unemployment and poverty rates. We are pleased to note from the buff that the fight against poverty remains at the center of the development agenda in order to address the population's large social needs and provide employment opportunities, especially for the youth. Efforts should continue to address infrastructure gaps, including electricity and transport issues, in order to boost inclusive growth.

With these comments, we wish the authorities further success in their reforms.

Mr. Mohan and Mr. Govil submitted the following statement:

We thank staff for a comprehensive set of papers for the Article IV consultations with the Islamic Republic of Mauritania and Mr. Yambaye and Mr. Sidi Bouna for their informative buff statement.

Mauritania recorded a rebound in growth in 2012, which continued for two more years supported by high iron ore prices and significant donor assistance. The staff projects that the growth momentum is likely to be sustained for the next few years—despite a decline in international iron ore prices—on account of improvements made in macroeconomic management.

We commend the authorities for their efforts towards increasing taxation revenues. The non-extractive tax revenues have increased by more than 50 percent during the past four years. Despite unfavorable external circumstances, the growth momentum in taxation needs to be maintained by undertaking further reforms in taxation. Nonetheless, we agree with the authorities' reservations about staff's recommendation for adoption of a fiscal rule for managing mining wealth. As Mauritania is a low income country with considerable basic social infrastructure needs, immediate implementation of the fiscal rule could be counterproductive and delay the implementation of development plans.

For the broader economy, the increasing gap between the domestic savings and investment ratios, that is funded by external resources (mainly FDI), is a matter of concern. Gross investment increased from 39.2 percent of GDP in 2010 to a high of 57.3 percent in 2012. On the other hand, gross savings are generally falling, from a high of 34.9 percent in 2011 to around 20 percent (projected) in 2016. At the same time, the current account deficit (CAD) has jumped up from 5.1 percent of GDP in 2011 to 26.1 percent in 2012. The CAD is expected to remain around this level during the next few years; even if it is financed largely by relatively stable FDI inflows, the high level of CAD makes the economy highly vulnerable to foreign developments, which can be sources of instability. The staff is requested to comment on the authorities' plans to finance the CAD in the medium-term. Further, given the uncertainties surrounding the future commodity prices and the large import-burden created by FDI financed projects in Mauritania, we are skeptical about staff's projection that by 2021 the CAD would reach a long-term steady state figure of 6 percent. The staff's comments are welcome about the feasibility and risks associated with their long-term projection for CAD.

We had earlier raised concerns about the disconnect between technical difficulties experienced by the mining sector during 2012 and the large FDI inflows being invested in the same sector. In their gray statement, Mr. Yambaye and Mr. Sidi Bouna have attributed the significant adverse impact on the external sector in recent times to the deterioration in the terms of trade and the large FDI related imports. As per staff estimates, during 2013-19 the iron ore production would triple and the iron ore prices would remain subdued. This could lead to an unhealthy persistence of the external sector vulnerabilities. We would appreciate staff's assessment of the likely increase in the FDI related imports on account of such tripling of the iron ore output, and its impact on the external sector vulnerability. Does the economy have sufficient absorptive capacity that would allow it to make productive use of the likely FDI inflows?

The risk of debt distress has increased (from moderate to high) on account of the increase in Mauritania's public debt from 73.7 percent of GDP in 2013 to an estimated 78.4 percent in 2014. With subdued growth in the trading partners and lower commodity prices, fiscal stresses are likely to remain high during the next few years, and we urge the authorities to maintain a fiscal stance consistent with debt sustainability. More progress on subsidy reforms—for fuel, electricity and food—is needed. The public sector wage bill also needs to be contained. Targeted social transfers to low-income households would help in employing government resources in a fiscally sustainable way. Could staff state the timeline for completion of the household survey being conducted for this purpose, the mechanism that would be used for transferring such subsidies to the poor households, and the scope of the project (i.e. what types of subsidies and what fraction of total subsidies would be targeted in this manner)?

We agree with staff recommendation about the need to strengthen the monetary policy framework, and note that the authorities have agreed about the need for reestablishing the use of more direct and traditional liquidity management instruments such as interest rates and reserve requirements, and limit the use of indirect instruments like foreign exchange interventions and treasury bills. We support the authorities' view that given Mauritania's very shallow foreign exchange market, characterized by considerably higher demand over supply, the liberalization of the foreign exchange market should be undertaken in a calibrated manner.

With these comments, we wish the authorities all success in their development efforts.

Mr. Sun, Ms. Ai and Ms. Li submitted the following statement:

We thank staff for the comprehensive set of reports and Mr. Yambaye and Mr. Sidi Bouna for the useful buff statement. With the support of the ECF arrangement, Mauritania continues to register strong economic growth, with improved fiscal and external buffers, and contained inflation. Meanwhile, the country is experiencing strong headwinds from the unfavorable global environment, and vulnerabilities in the external and banking sectors call for increased attention. We agree with the thrust of staff's appraisal and would like to confine ourselves to the following comments.

In view of the shortfall in mining revenues and the debt risk, more efforts are needed to improve fiscal sustainability. Although the extractive revenue losses might be partly offset by the increase in VAT revenue, the growth prospects weigh on future tax collections. Considering the large development investment needs, we encourage the authorities to make additional efforts to mobilize more fiscal revenues by broadening the tax base and improving tax administration. Mauritania's risk of debt distress has downgraded from moderate to high, due partly to the technical reclassification by the World Bank. Given the increasing debt level, it is desirable for the authorities to improve the debt management capacity, with TA support from the Fund and others.

Close attention to the financial health of the banking system is warranted. Although the banking sector is well capitalized and liquid, it remains vulnerable due to high credit concentration, large foreign exchange risk exposure, and low asset quality. We commend the authorities for their series of concerted measures to improve the financial regulatory framework, but more needs to be done to enhance regulatory enforcement. Moreover, the banking resolution framework could be further strengthened to address the troubled banks, and the central bank should be equipped with more lender-of-last-resort tools. We welcome the authorities' intention to introduce early warning solvency and liquidity indicators while reinforcing the deposit guarantee fund.

The persistently high unemployment and poverty call for structural reforms to bolster a more inclusive and equitable growth. We commend the authorities' efforts in promoting private sector development and economic diversification, as well as ameliorating the business climate. Complementary efforts to improve education and the labor market would be desirable so as to facilitate job creation. Initial progress has been made in targeting social transfers, and we encourage the authorities to continue this work with support from the World Bank and other institutions.

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

Mr. Çanakci and Mr. Repansek submitted the following statement:

We welcome the informative reports on Mauritania and broadly agree with staff's appraisal. We would like to provide the following comments for further consideration.

We recognize Mauritania's high growth and improved macroeconomic stability, which were restored with the help of the 2010-2013 Extended Credit Facility Arrangement. However, the external imbalance and financial system vulnerabilities remain challenging risks. Additionally, economic diversification is slow and is hampered by insufficient investment in human capital.

Broadly, we see a risk to medium-term growth sustainability and macroeconomic stability in the gap between Mauritania's relatively high economic growth and abundant natural resources on one hand, and the unfavorable human development and business environment indicators on the other. We believe that paying additional attention to this risk is warranted. We welcome that the fight against poverty and improvements in the business environment remain a priority of the authorities' policy agenda, as Messrs. Yambaye and Sidi Bouna emphasized in their buff statement. We also welcome that the risk matrix identifies political and/or social unrest as a source of risk, and note that this could materialize through a lack of improvement in the living standards. Given that the risk is assessed as low, additional information on the indicators behind this assessment would be appreciated.

Mauritania's fiscal policy appears to be prepared to absorb the negative consequences of the deterioration in the 2014-16 terms of trade. We recognize the substantial increase in non-tax revenues in recent years that make this kind of policy response easier. However, given that the 2015 revenue projections are on the optimistic side, we would encourage the authorities to impose corrective measures to prevent fiscal slippage in a timely manner, should it become necessary. We support the recommendations on strengthening medium-term fiscal sustainability, but emphasize that capacity-building warrants particular attention. In the context of medium-term fiscal projections, we wonder how much space could be made available for an increase in education and health care expenditures. The staff's comments would be appreciated.

The monetary policy stance has served the country well, but constraints justify an expansion of the policy tool kit. In that respect, a decisive but careful approach is warranted to prevent an inflation rate increase. Exchange rate policy should be used for shock absorption, and external buffers should be rebuilt. The recent strengthening of the U.S. dollar against other major currencies is another argument for the gradual foreign exchange market liberalization which we support. We recognize that the authorities have demonstrated their commitment to meeting their obligations under Article VIII through eliminating three multiple currency practices and two exchange restrictions. We note that the remaining exchange rate restriction does not discriminate among Fund members, that staff considers it necessary for balance of payments reasons, and that it is temporary. Therefore, we can support the authorities' request for this restriction to remain in place for no longer than one year.

The financial sector is shallow and underdeveloped, but the recent significant increase in competition is welcome. The Financial System Stability Assessment (FSSA) spells out substantial weaknesses in the system and recommends how to address them. The authorities' commitment to the implementation of the recommendations is welcome, but this complex task requires careful prioritization and coordination among stakeholders, alongside strong capacity building.

Banking sector regulation and supervision need further improvement given that risks in the sector are substantial and widespread. Removing the license of one undercapitalized bank was a step in the right direction, and other similar cases should follow. In particular, the authorities should act swiftly in the case of the Deposit and Development Fund, an undercapitalized and unsupervised public bank. Furthermore, the proper supervision of the National Health Insurance Fund and the National Social Security Fund should also be established with no further delay. Finally, along with the 2007 FSAP primary recommendation, groups affiliated with weak banks should be required to recapitalize them and consider mergers.

A well-developed, financially sound, well-governed and supervised microfinance sector could substantially boost financial inclusion and SME sector development. The FSSA revealed a set of significant microfinance sector weaknesses, and further discussion is warranted on how to eliminate them.

Structural reforms to facilitate the promotion of inclusive, private sector-led growth are critical to Mauritania's development. We agree with the key elements of the challenging reform agenda (paragraph 25 of the staff report). The policy steps taken thus far are in the right direction, but appear insufficient. Should the authorities request, given the Fund's mandate, expertise, and the policy challenges identified in Mauritania, technical support should focus on the areas of monetary policy, the exchange rate regime, and financial sector development. We encourage staff and the authorities to intensify dialogue with other stakeholders in the international community on how to accelerate and prioritize structural reforms focused on key elements of the reform agenda.

We support education as a priority of the policy agenda. The information in the selected issues paper on the informal sector reveals daunting challenges in this area, but also presents commendable efforts for gender gap reduction and gender equality promotion that should continue.

Mr. Sterland, Mr. Moon and Mr. Togmid submitted the following statement:

We thank staff for their comprehensive reports and Messrs Yambaye and Sidi Bouna for the informative buff statement.

We welcome the strong macroeconomic performance of the Mauritanian economy over the past few years, mainly supported by the mining sector developments. However, given the sizable downside risks such as adverse terms of trade shocks, further steps are needed to achieve sustainable and inclusive growth through strengthening fiscal framework for sustainability, facilitating financial sector development and further implementing structural reforms. We agree with the thrust of staff's appraisal, and would like to limit our comments to the following points:

Strengthening fiscal framework is crucial. We welcome the measures to broaden the tax base, improve tax collection, and overhaul the tax administration, which contributed to substantial increase of budget revenues from non-extractive sectors. However, the budget's high dependence on volatile mining revenues and deteriorating risk of debt stress pose challenges to fiscal management in the medium term. Therefore, we urge the authorities to maintain fiscal consolidation to create buffers and to preserve medium-term sustainability. We would welcome staff's explanation on how a fiscal framework including a fiscal rule would affect the implementation of Mauritania's development agenda, which includes considerable economic and social infrastructure needs.

Financial sector needs to be further developed. We note the findings in the FSSA report and welcome the authorities' commitment to implementing the recommendations. Further strengthening bank's capitalization, improving supervisory framework, and promoting financial inclusion would help achieve a more stable and inclusive financial system.

Accelerating ongoing structural reform is critical. Given the weak infrastructure and longstanding structural bottlenecks, we encourage the authorities to accelerate structural reforms, through building appropriate infrastructure and improving the business climate. We also urge the authorities to make further efforts to foster growth, promote job creation and reduce poverty. Effective implementation of the action plan under private sector development strategy is welcome.

Ms. Meyersson and Ms. Jonsdottir submitted the following statement:

The Islamic Republic of Mauritania will need to build on previous years' strong macroeconomic policies as well as structural reforms to weather negative price developments in the country's main export industry. We thank staff for the comprehensive reports where the common thread is a call for a strengthening of institutions, whether associated with public administration, debt management or the financial sector. We agree in the main with staff's policy advice but have a few additional remarks for emphasis.

The authorities should weigh carefully whether to move forward with investments in the mining sector or prioritize other infrastructure investments that could underpin further diversification of the economy. As staff has pointed out, iron ore prices could decline below the level used in the baseline which would put further strain on the budget as well as compromise the profitability of further investments in the sector. The staff puts forward a very convincing argument in favor of increased education spending, where the level is low compared to peers, as well as underlining the need for infrastructure investments with respect to water, electricity and transport. In general, further rationalization of public investments could bring better results and important savings.

A more robust fiscal framework for managing resource wealth is a necessary objective given the significant impact of external shocks. We note from Mr. Yambaye and Mr. Sidi Bouna's balanced buff statement that the authorities are concerned that implementing a fiscal rule in a country with significant social infrastructure needs could weigh on the authorities' development agenda. In our view, staff's suggestion for a fiscal rule targeting a non-resource primary balance for longer-term stability with some frontloading of targeted public investment, could be considered for the medium term. In the meantime, the establishment of a development fund, stringent prioritization of public investments and careful multi-year planning should be considered for the short term. Could staff comment further on the contents of the Organic Budget Law under discussion in parliament and the prospects for it being passed the first half of 2015?

The current environment of low inflation should be used to strengthen institutions and governance for the conduct of monetary policy. In this context, a recapitalization of the Central Bank of Mauritania should be implemented, and a more efficient liquidity management framework established. As reserves are declining, increased exchange rate flexibility might be considered to aid in absorbing external shocks. We take positive note of the authorities' intent to eliminate all remaining exchange restrictions within the space of one year.

Mr. Mozhin and Mr. Vasilyev submitted the following statement:

We thank staff for a set of well-written papers and Mr. Yambaye and Mr. Sidi for their helpful buff statement. Restored macroeconomic stability and improved terms of trade in the previous years had supported Mauritania's robust growth. Continuing uncertainty in the world economy brings downside risks through iron ore price dynamics and external financing conditions. Fiscal and monetary policies need to take advantage of currently favorable conditions and protect the economy against possible shocks. We broadly agree with the thrust of the staff appraisal and would like to make the following comments for clarification and emphasis.

Fiscal measures should help absorb negative shocks and reduce volatility. As a resource-rich developing country, Mauritania can benefit from the adoption of the fiscal rule and stabilization fund in the medium term. Eventually such a measure can insure the budget and economy as a whole against volatility in iron ore prices. We share staff's view that the budget should recognize the transfers to the public electricity company in order to advance fiscal transparency. We commend the authorities for their recent success in improving tax revenue. Further efforts in revenue mobilization, oil windfall revenues and prudent debt management should offset possibly large near-term reduction in mining revenues.

The DSA analysis delivers an important message to the authorities and highlights the limitations associated with the use of the World Bank's Country Policy and Institutional Assessment (CPIA) index. The threshold for Mauritania's sustainable debt went down due to low CPIA scores in 2011-2012. The staff mentioned in the second footnote (page 5, the DSA report) that Mauritania would have maintained moderate risk of debt distress if only current CPIA rating was used. Although we understand that quality of institutions does not fluctuate often, a 3-year moving average, perhaps, is not even the second-best solution, given that it always shows turning points with a delay. The DSA report would become clearer if the information from the second footnote was introduced in the summary on the first page of the DSA as a caveat for its outcome. However, we encourage the authorities to take into account the DSA results: the risk of debt distress will be manageable if the authorities continue to preserve higher quality of institutions. Could staff comment on the exposure to regional Arab lenders in light of the oil price drop?

The central bank has an opportunity to upgrade monetary policy framework, given currently low inflation. We welcome the authorities' intentions to enlarge liquidity management tools. It will be a step towards lower FX intervention and higher exchange rate flexibility. The report mentioned risks stemmed from gradual depreciation vis-à-vis the U.S. dollar, given the strengthening of the U.S. dollar against other major currencies. Could staff comment on the impact of further developments in this area in light of the announced European QE?

The central bank should continue to strengthen the banking sector through consistent policies to enforce existing regulatory framework, increase banks' capitalization, and improve liquidity. Existing institutional shortcomings create fundamental problems. Inadequate protection for the BCM staff in the conduct of their duties coupled with growing risks, such as connected lending above the limits, lead to a loss of confidence and expose deposit insurance scheme.

Mr. Chodos and Mr. De la Barra submitted the following statement:

The economy of Mauritania has been growing impressively in recent years. Mauritania's mining sector is enjoying a favorable momentum as investment is flowing to the sector even though the projected growth rate would be smaller than 2014's. The outlook for 2015 is still positive and encouraging which would allow the country to continue building the resilience of the non-mining output. However, policies have to be carefully designed to preserve the macroeconomic stability and counteract the downside risks, as commodity prices are declining in the international markets, as mentioned clearly in Box 2 and in the Risk Assessment Matrix, which identify the high likelihood and impact from some of the risks for Mauritania.

The staff's advice on the need for diversification in the economy in Mauritania is appropriate but it would be more helpful if such advice indicates to what sector or industries the Mauritanian economy should make their efforts for diversification. We welcome the authorities concerns and recognition about the impact of the downside risks, particularly the increasing external risks that imply higher vulnerability because of trade shocks which would jeopardize the hard-won macroeconomic stability gains.

We commend the significant increase in tax revenue coming from sources other than extractive industries, which strengthens the fiscal policy stance. It is highly positive that the level of formalization of the economy has been increased by the strong performance in VAT levied on the mining sector. It is also commendable that Mauritania has been able to protect its extractive industries tax base given the low levels of royalties (by international standards) collected from the mining companies.

Given the high risk of further decline in iron-ore prices, we tend to agree with staff's recommendations regarding the use of buffers, concessional financing and rebalance spending in the short term, in order not to end up with a greater fiscal deficit, which has widened compared to 2013. The authorities should preserve the fiscal stability. While we understand the authorities' preference for not adopting a fiscal rule at this time, we are encouraged by the prospects seen by the authorities to discuss this issue in the future as Messrs. Yambaye and Sidi Bouna state in their buff statement. The infrastructure gap in Mauritania is considerable as in other low-income countries and the authorities want to address this pressing issue. However, the fiscal expenditure items should be carefully prioritized in order to maximize the returns and get a greater output base in the near future. Setting up a stabilization fund out of the income coming from extractive industries in operation is appropriate and should be considered by the fiscal authorities for it to avoid incurring in higher fiscal deficit if fiscal income is affected a great deal by the decline in mineral prices.

The monetary instruments should be enhanced to reign on excess liquidity in the banking sector. We are of the view that the central bank authorities should resume using the policy rate and reserve requirements as to strengthen the monetary policy framework, given that relying only on foreign exchange interventions may reach a limit since international reserves would get lower and close to the threshold.

We support the staff recommendation about reforming the foreign exchange market and initiating better coordination between the monetary and exchange rate policies. We support the proposed decision in regard to the Article VIII of the Articles of Agreement.

We note that banking institutions although enjoying a high capital ratio in the aggregate, are subject to a number of risks. One of which is the credit risk as the non-performing loans (NPLs) are at a high level which is worrisome and there is presence of connected lending. Liquidity risk is also a matter of concern as identified in the report.

We commend the central bank's willingness to revise the existing framework for banking resolution, as well as to provide further protection to the authorities and employees in their supervisory duties. Improvement in the quality of financial services and inclusion would support credit for private investment. The 2014 FSSA has identified key issues related to the central bank, financial stability, monetary policy, monetary markets and exchange rate market which contain measures of high priority and urgency. We encourage the Mauritanian authorities to take due consideration to the recommendations proposed in the FSSA report.

We welcome the initiative to better target the social transfers for the benefit of the poorest and efforts to improve the business climate. It is necessary for Mauritania to continue strengthening the institutional framework of public institutions, with an emphasis on public enterprises. In the same vein, human capital building and enhanced business climate would help to reduce unemployment and depart from the dependence on extractive industries.

With these comments, we wish the Mauritanian authorities the best in their endeavors.

Mr. Santoso, Mr. Marcelo and Mr. Kharel submitted the following statement:

We thank staff for the candid report and Messrs. Yambaye and Sidi Bouna for their informative buff statement. We are pleased to note Mauritania's resilient growth and significant improvements in achieving the MDG goals while restoring macroeconomic stability, supported also by the recently completed ECF arrangement (2010-13). The medium-term outlook remains encouraging but downside risks remain given high debt distress and deteriorating foreign exchange reserves. While the banking sector is well capitalized and liquid, vulnerabilities could emerge due to low profitability and weak asset quality in the banking sector, as highlighted in the FSSA report. In this context, we commend the authorities for their firm commitment towards fiscal consolidation and continuing structural reforms in key areas so as to foster high and inclusive growth and reduce poverty while preserving macroeconomic stability.

Prudent fiscal and public debt management policy is critical to strengthen debt sustainability while enhancing inclusive growth. In this context, we welcome the authorities' fiscal consolidation measures adopted in the 2015 Budget that includes increasing the VAT rate and containing recurrent expenditure. However, given the unsustainable debt trajectory and building up pressure in the foreign exchange reserves, we agree with staff that further measures to broadening the tax base, improving tax collection capacity, curbing current expenditure by mainly proactively managing the wage bill, gradually phasing out subsidies to public sector entities, improving public enterprise operations, and enhancing the efficiency of capital spending should remain key priorities.

We welcome the authorities' broad agreement with FSSA recommendations. While we note that the overall banking sector has remained liquid and well capitalized, vulnerabilities have emerged due to still high NPLs and low profitability. In this context we agree with staff that ensuring the operational independence and accountability of the central bank, strengthening banking supervision, strict enforcement of existing regulation and removing rigidities and distortions in the foreign exchange market should be the immediate priority. We encourage the authorities to take further action to promote financial inclusion and create an enabling policy and regulatory environment for microfinance and Islamic finance. We also welcome the planned development of new monetary policy instruments to strengthen liquidity management and monetary transmission. We encourage the authorities to address the remaining rigidities in the AML/CFT framework so as to build up confidence in the banking sector.

Accelerating structural reform is crucial to foster inclusive growth. Given low productivity and deficiencies in achieving some of the key MDG targets including poverty reduction, it is imperative to overcome the long-lasting structural bottlenecks and improve business environment as stated in the staff's report while protecting the most vulnerable. In particular, as we note that Mauritania ranks at 173 out of 189 in the World Bank's 2014 Business indicator, we agree with the staff that strengthening transparency, governance and institutions are key to support broad based and inclusive growth.

Finally, we support the authorities' request to temporarily maintain the remaining exchange restriction, which staff deems necessary for balance of payments reasons. We look forward to the eventual elimination of the exchange restriction in 2016 as part of the the authorities' commitment to meet Mauritania's obligations under Article VIII of the Fund's Articles of Agreement.

With these remarks, we wish the authorities and people of Mauritania every success for their future endeavor.

Ms. Kapwepwe and Mr. Tucker submitted the following statement:

The steadfast implementation of prudent macroeconomic and structural policies, within the context of a Fund-supported program, has helped Mauritania achieve macroeconomic stability and sustain economic growth at high levels over recent years. While the authorities have accumulated sizable external and fiscal buffers supported by a favorable external environment, the near-to-medium term outlook is nonetheless challenged by adverse commodity price shock and weakening external demand. Going forward, policies should focus on mitigating these emerging external vulnerabilities and addressing poverty by rendering growth more inclusive. In this regard, we welcome the authorities' commitment to stay the course with sound macroeconomic policies and implement necessary structural reforms, and are reassured by Mr. Yambaye and Mr. Sidi Bouna's insightful buff statement. We broadly agree with the thrust of the staff report.

Persevering with Fiscal Consolidation and Preserving Debt Sustainability

The authorities' effort at pursuing fiscal consolidation aimed at maintaining the sustainability of public finances over the medium term is commendable. We consider the fiscal adjustments in the 2015 budget, notably the increase in the VAT rate and rationalization of recurrent spending, appropriate in addressing the gap envisaged from a decline in extractive revenues.

There is however the need for a more enduring solution to the country's excessive dependence on revenues from the extractive industry which clearly is a growing source of fiscal risk. To this end, we concur with staff on the importance of adopting an appropriate fiscal anchor to effectively manage natural resource revenues. We nonetheless see merit in the authorities' view, articulated in the buff statement, that implementation of such a fiscal rule should not distract from urgently addressing daunting development and social challenges.

It is concerning to note that the country is now assessed to be at a high risk of debt distress on account of weakened institutional capacity. Efforts to strengthening debt management capacity should thus be expedited. Moreover, continued reliance on concessional financing and refrain from non-concessional external borrowing, including collateralized borrowing against future mineral revenues, remains crucial.

Enhancing the Efficacy of Monetary and Exchange Rate Policies

We concur with staff that current monetary conditions present an opportunity to strengthen the monetary policy framework, including by adopting a formal liquidity forecasting framework, expanding the array of monetary instruments at the disposal of the central bank, and obtaining a better understanding of the monetary policy transmission mechanism. It is also of immense importance that the central bank be recapitalized to ensure its operational autonomy and effectiveness. On exchange rate policy, the focus should be on enhancing the flexibility of the exchange rate to help absorb exogenous shocks, and on rebuilding foreign reserves to support external stability. We welcome the authorities' commitment to address exchange restrictions to ensure compliance with obligations under Article VIII, and support the proposed decision to retain the remaining exchange restriction for the next one year.

Accelerating Critical Structural Reforms

While Mauritania has succeeded in sustaining growth at high levels in recent years, rendering this growth inclusive to positively impact poverty outcomes has been a daunting challenge. We thus support the authorities' envisaged reform agenda that aims to address the underlying structural impediments to growth alongside emerging external risks. Steadfast implementation of the private sector development strategy is needed to create a conducive business environment and increase employment opportunities. More importantly, determined effort is required to diversify the economy outside of the extractive sector to ensure that growth is sustained over the long term.

Mr. Alshathri and Mr. Abdel-Rahman submitted the following statement:

We thank staff for concise reports and Mr. Yambaye and Mr. Sidi Bouna for their informative buff statement. We broadly agree with staff assessment, and we would like to make few points.

We note that Mauritania faces important challenges and the economic outlook is subject to considerable downside risks. Nonetheless, we are encouraged by the authorities' commitment, as articulated in Mr. Yambaye and Mr. Sidi Bouna's buff statement, to continue to work closely with the Fund and other development partners to put in place the necessary policies to address these challenges and consolidate the macroeconomic stability gains achieved in recent years. In the same vein, we encourage the authorities to step-up their efforts to implement the needed structural reforms to enhance the economy's resilience to shocks, and to promote more sustainable and inclusive growth.

We note that Mauritania's imports are dominated by capital goods, which are tied to the mining activities and funded by FDI, followed in the order of importance by petroleum and food products. On the other side, exports are dominated by commodities, mainly iron and copper. Given the composition and the nature of Mauritian's merchandise imports and exports, we would welcome staff reactions to the following points:

Should the impact of the decline in iron ore price be mitigated by a higher decline in price of oil and food imports? We wonder if annualizing the current account deficit in the first half of 2014 is an informative indicator, given that oil prices took completely two different directions in the two halves of the year. Similarly, we wonder if the weakening in current account and decline in reserves in 2013 and first half of 2104 is actually reflecting the impact of high oil prices, and this should be reversed going forward once the impact of the recent decline in oil price starts to kick in.

The large external financing gap estimates envisaged under the downside scenario with no mining expansion (Box 2) do not seem to reflect that imports are dominated by capital goods that are tied to the mining activities and funded by FDI, which should help mitigate the impact of this shock on the external balance.

At the current juncture, we see merits in the authorities' calibrated approach to the use of the exchange rate as a shock absorber and the use of fiscal and external buffers in a counter-cyclical fashion. We are of the view that staff recommendation to allow for a bigger role of exchange rate as a shock absorber should take in to account the structure of imports and exports, and the state of development of domestic foreign exchange market. The structure of Mauritania's imports and exports would make the trade balance less elastic to exchange rate movements, hence, faster pace of currency depreciation most probably will be reflected in a higher domestic inflation, which would harm the poor and offset the impact of the nominal depreciation on the REER. Furthermore, a faster depreciation while the domestic foreign exchange market is still shallow could trigger unwarranted exchange rate overshooting.

We note that fiscal policy faces double challenges. In one hand, the high level of debt to GDP would call for fiscal consolidation to preserve fiscal sustainability. On the other hand, the authorities may need to increase spending to address infrastructure bottlenecks, eradicate poverty, and make further progress on the MDGs. In this regard, we welcome measures undertaken by the authorities in recent years to enhance non-mining tax revenue collection and contain the growth in noncritical recurrent expenditure areas, and we encourage the authorities to sustain fiscal reform to further strengthen revenue administration and promote the efficiency and productivity of fiscal resources allocation. While we see merits in staff recommendations to implement fiscal rule and fiscal anchor, we share the authorities view that focus should be on putting in place the needed prerequisites for the rule to work, and we invite staff to elaborate on the type of fiscal rule that could serve Mauritania’s needs to preserve fiscal sustainability while providing room for countercyclical response and critically needed spending to boost potential growth and eradicate poverty.

While we see merits in staff recommendations to develop the tool kit for excess liquidity management, we are of the view that priority should be given to recapitalizing the central bank in order to enhance the credibility and effectiveness of the central bank measures in managing domestic liquidity.

Finally, we welcome the authorities’ reiterated commitment to implement the FSSA report recommendations according to the agreed timeframe to address financial sector vulnerabilities.

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

Mr. Jimenez Latorre and Mr. Cova submitted the following statement:

At the outset, we thank staff for their informative set of papers, as well as Messrs. Yambaye and Sidi Bouna for their insightful buff statement. We broadly agree with the thrust of the appraisal and welcome the Mauritanian policy makers’ commitment to follow up the downside risks to the economy stemming from the external environment, since the outlook could potentially be compounded by not only a weaker demand from major trading partners, but also by the vagaries of iron ore international prices.

In particular, we recognize the significant challenges to macroeconomic stability, inclusive growth and debt sustainability, including shortfalls in improving debt management capacity and delays in strengthening the institutional framework. Faced with prospects of downside risks mainly linked to external developments and adverse climatic conditions that could affect the economic dynamics going forward, to count on the appropriate toolkit is crucial.

Nonetheless, we are reassured by the authorities' willingness to adopt further measures appropriate to deal with adverse developments. In this context, we encourage them to undertake comprehensive reforms consistent with the objectives of consolidating macroeconomic and financial stability, facilitating more inclusive growth, as well as promoting social inclusion. Articulating these objectives within a coherent broad strategy will improve the prospects of success.

The authorities' intention to strive for structural reforms and economic diversification for inclusive growth, while supporting the financial sector and the real economy through macroeconomic, structural and institutional factors, is commendable.

Likewise, bearing in mind the trade-off between the hypothetical implementation of a fiscal rule and its repercussions in terms of the development agenda reveals policymakers' sensitivity to the social consequences attributable to potential political and social unrest. Against the backdrop of lingering poverty, high unemployment rates, ageing population and rising inequalities, among other stalled social indicators, we wonder whether the current safety nets are sufficient to provide a good level of social protection. From staff's perspective, what additional measures, if any, could the authorities consider to overcome shortcomings in this area to improve living standards?

We take note of the assessment regarding the, broadly speaking, sources of vulnerabilities and constrained conditions under which the banking system performs. In this connection, we welcome BCM's active steps taken to protect the system from shocks. However, more can be done; particularly, for addressing fragilities linked to the regulatory framework enforcement, including through the possible extension of both the legal scope and the financial system supervision's perimeter, in line with the implementation of the FSSA roadmap.

On the basis of the previous remarks, we praise the authorities for their achievements and wish them success in further advancing their economic and social policy agenda.

Mr. de Villeroché submitted the following statement:

We thank staff for the comprehensive set of papers as well as Messrs. Yambaye and Sidi Bouna for their insightful buff statement. We take positive note of Mauritania's good growth performance in 2013 and 2014, which has been accompanied by progress in structural reforms. In particular, the Extended Credit Facility program (2010-2013) paved the way for restoring macroeconomic stability, improving the fiscal position and building buffers. However, many challenges remain. In particular, growth continues to be insufficiently inclusive and Mauritania faces the challenge of being highly dependent on the mining development and food imports. The current volatility in commodity prices (the decline in iron ore prices in particular) and possible shifts in global demand for metals underline the needs for putting in place safeguards to protect the economy from boom and bust cycles and maintain debt sustainability.

We broadly agree with staff's assessment and recommendations in favor of a cautious macroeconomic policy, aimed at mitigating risks to external shocks in a context of higher risks on indebtedness and deterioration of terms of trade. We would like to offer the following comments.

Mauritania, endowed with mining resources, has a potential to achieve strong growth in the medium term. In the context of the decline in commodity prices, does staff have information on a potential investments freeze in mining and hydrocarbons sector? Do you estimate the ambition to double mining production by 2020 achievable? The diversification of the economy should remain paramount. We welcome the authorities' commitments to improve the business climate in order to boost the role of the private sector. As underlined in the Financial System Stability Assessment, the consolidation of the regulatory and supervision framework would represent a step to increase financial inclusion and strengthen the stability of the banking sector. Unemployment and weak capital development also need to be tackled as part of the authorities' reforms.

We commend the authorities for their success in increasing fiscal revenues and efforts to contain current expenditure. We encourage them to continue implementing their long-term fiscal consolidation strategy and strengthen fiscal discipline. In particular, the macroeconomic situation of the country will continue to depend, in part on the performance of the mining sector, at least in the short term. Efficient management of the resources will continue to be key for ensuring the fiscal stability and preserve macroeconomic stability. The pursuit of the technical assistance from the Fund and the World Bank will be crucial in the area.

The debt sustainability analysis deteriorated with Mauritania now at high risk of debt distress. This results mainly due to the lagged impact of the low CPIA score received in 2011. While the authorities have made progress to strengthen the quality of policies and institutions, we would like to strongly encourage pursuing the efforts. Having said that, we note that the public debt increased in 2014 as the country has embarked on an ambitious program of investments to improve infrastructures. We concur with staff on the importance to well identify the magnitude of the infrastructure gap and establish a multi-year investment program. The debt vulnerabilities underscore the need for Mauritania to mainly rely on concessional financing and that agreement is reached rapidly on outstanding debts. We are concerned by the still unsettled Kuwaiti debt relief under the HIPC terms, which is highly detrimental for external debt sustainability.

Mr. Catsambas and Mr. Temmeyer submitted the following joint statement:

We thank staff for a comprehensive set of papers and Mr. Yambaye and Mr. Sidi Bouna for an informative buff statement. We commend the authorities for their success in restoring macroeconomic stability that laid the basis for a strong growth performance over the past few years. Thanks to the authorities' tax efforts, the rapid growth experienced in Mauritania's extractive sector has benefitted domestic revenues and the fiscal balance. At the same time, strengthening the fiscal framework is of the utmost importance in light of possible revenue shortfalls and the high risk of debt distress. Vulnerabilities related to further deterioration in the terms-of-trade against the backdrop of high current account deficits need to be thoroughly addressed by policy adjustments. Implementation of structural reforms aimed at improving governance, the business climate, and the quality of institutions is vital in order to facilitate the needed diversification of the economy, enable robust private sector-led growth, and improve living standards and social indicators.

We broadly support staff's analysis and policy advice and offer the following comments.

We underline the recommendations in the staff report on measures to buttress medium-term fiscal sustainability, particularly with regard to budget transparency. While we welcome changes in the petroleum price structure whose adjustment formula should translate into significant windfall revenue from lower oil prices this year, we urge the authorities to register these revenues appropriately in the fiscal accounts. In addition, we take note of the anticipation of substantial revenues from the renewal of telecom licenses (which according to staff projections yield a decline in the current account deficit from 24.7 percent in 2014 to 7.7 percent this year), we agree with staff that these revenues should be, partially, used to reduce Mauritania's stock of outstanding debt. In this context, we also echo the advice from staff and many directors to refrain from nonconcessional external borrowing including collateralized borrowing against future mineral revenues.

Macroeconomic stability and fiscal policy formulation would benefit from an improved fiscal framework that appropriately accounts for Mauritania's extractive sector. To this end, we encourage the authorities to undertake steps toward the adoption of a fiscal rule and creation of a fiscal stabilization fund that will enhance intergenerational equity while providing buffers against commodity price volatility. We welcome the useful role that the Fund can play in this regard by giving policy advice informed by its cross-country work on resource rich developing countries.

We encourage the authorities to strengthen the monetary policy framework and enhance exchange rate flexibility to enable the rebuilding of external buffers. While acknowledging the challenges associated with the lack of a deep foreign exchange market, we agree with staff that it is essential to increase the role of the exchange rate as a shock absorber, given adverse terms-of-trade developments.

On the structural side, we welcome staff's very thoughtful SIPs on employment, economic diversification and inclusive growth. We consider that these papers provide policy recommendations that could be valuable inputs for policy discussions in Mauritania.

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

We thank staff for the comprehensive report and Mr. Yambaye and Mr. Sidi Bouna for their insightful statement.

In a challenging environment marked by persistent external uncertainties, Mauritania's has maintained the momentum of solid growth and subdued inflation, bolstered by high iron ore prices and increasing public investment, This performance owes much to the authorities' continued commitment to preserving macroeconomic stability and stepping up structural reform implementation to promote high and inclusive growth. While the outlook is favorable, Mauritania is highly exposed to external shocks. The decline in iron ore prices and the downward revisions to growth in advanced and emerging economies pose significant challenges, and additional efforts are needed to diversify the economy and further build fiscal and external buffers against potential shocks. We concur with the thrust of the staff appraisal.

We commend the authorities for their fiscal consolidation efforts in recent years, including the remarkable improvement in tax revenue collection, even though these efforts were not effective in improving the non-extractive fiscal balances and curbing the upward trend of public debt. We welcome the tax and revenue measures taken by the authorities to mitigate the shortfall in the mining revenue under the 2015 budget, as well as their intention to use fiscal buffers to smooth its impact. Going forward, we are pleased to note the authorities' recognition of the need for measures to further strengthen revenue mobilization, bring the wage bill under control and reduce transfers and subsidies, improve efficiency of capital spending, and strengthen public enterprise monitoring. An appropriate social safety net would be crucial to support these reforms. The staff recommends strengthening fiscal policy formulation to reduce reliance on mineral revenue, including through adoption of a fiscal rule and a fiscal anchor. However, the authorities are rightly concerned that such a framework could create unwelcome constraints on key social and infrastructure spending in a country with huge developmental needs. Could staff elaborate on how these reforms could be better adapted to a LIC environment?

While monetary policy has been successful in bringing inflation under control, recent increase in bank liquidity calls for strengthening the monetary policy framework and expanding monetary policy instruments. We welcome the shared vision of the authorities and staff on the way forward, and agree with the authorities on the importance of central bank recapitalization for increased credibility and effectiveness of monetary policy. We take note of staff indication that the exchange rate is in line with fundamentals, and agree on the need to strengthen the role of the exchange rate as a shock absorber, including in building further external buffers. The authorities' plans to gradually liberalize the foreign exchange markets are encouraging. We welcome the recent elimination of three multiple currency practices, and support their request for temporary Fund's approval of the remaining restriction, in view of their commitment to eliminate it within one year.

The framework for bank regulation, as well as for risk-based and on-site supervision has been recently strengthened. However, the financial sector remains shallow, and the banking sector remains fragile. Further reforms, as elaborated in the SSAA, including enhancing protection of supervisors, will be crucial for effective supervision. We welcome the authorities' intention to implement FSSA recommendations, as reiterated by Mr. Yambaye and Mr. Sidi Bouna.

The authorities are encouraged to step up structural reforms to enhance the economy's resilience and promote inclusive growth, including by diversifying the economy, improving productivity, and enhancing the business climate. This will be crucial for promoting job creation, reducing poverty, and achieving the MDGs. We welcome the progress made in these areas, including in targeting social transfers, addressing infrastructure gaps, and promoting financial inclusion and improving access to financial services, as highlighted by Mr. Yambaye and Mr. Sidi Bouna.

We share Mr. Yambaye and Mr. Sidi Bouna's concern regarding the recent downgrading of the Mauritania's risk of debt distress from moderate to high. This is to a large extent explained by the impact of the short-lived decline in capacity assessed in 2011, which affected the three-year rolling average, even though capacity has been strengthened recently. We note in particular that the three-year average CPIA score in 2011-13 at 3.24 was only very slightly below the 3.25 threshold triggering the reclassification. Did staff consider available room for flexibility to avoid this downgrade for such a tiny shortfall? Could the use of borderline concept help address the issue? When is the earliest opportunity for updating the CPIA rating to take account of recent improvements in capacity?

We wish the authorities further success in their endeavors.

The staff representative from the Middle East and Central Asia Department (Ms. Vera Martin), in response to questions and comments from Executive Directors, made the following statement:[1]

I would like to address two of the issues raised in Directors' gray statements, mainly on the scope of the exchange rate flexibility and the relevance of structural reforms, which are linked by the objective of increasing the resilience of the Mauritanian economy to external developments.

[1] Prior to the Board meeting, SEC circulated the staff's additional responses by email. For information, these are included in an annex to these minutes.

Reforming the foreign exchange market is needed to enhance exchange flexibility and support economic development over the medium term. The staff is working closely in designing the next steps, taking into account Mauritanian specific conditions. The foreign exchange market was first established in 2007 and the authorities took steps to establish a platform to determine the value of the currency through the fixing section.

In the context of the last Extended Credit Facility (ECF) program, and given favorable external conditions that allow for higher accumulation of reserves, the central bank intervention had eliminated foreign exchange rationing in the economy, and built up external buffers that have proven to be helpful in the current juncture.

The authorities’ steadfast implementation of foreign exchange measures recently has shown their commitment to meeting obligations under Article VIII and facilitated the promotion of further integration of the foreign exchange market, which remains highly segmented. We see the need for greater exchange rate flexibility in the short term to absorb the external shock and rebuild reserve buffers given the decline in global iron ore prices, Mauritania’s main export.

We also see a need for higher exchange flexibility because maintaining the current exchange rate regime in the context of upcoming European quantitative easing will erode external competitiveness. Directors highlight the need to take into account shallow exchange markets at the moment to ensure gradual flexibility. We will work with the authorities on ensuring or supporting gradual flexibility of the exchange rate.

Over the medium term, exchange rate flexibility will require deepening of the foreign exchange market and the development of an interbank market, so that it can play a bigger role in supporting economic diversification and private sector development. This will require reducing market imperfections like leveling the playing field for foreign exchange access by the private sector, increasing predictability of central bank intervention, and enhancing banks’ capacity to assess foreign exchange risk.

With regard to the broad structural reform agenda, we see this as a medium-term strategy to strengthen the resilience of the economy to external shocks. The authorities’ agenda to promote private sector development is focusing on upgrading the value added for sectors that they have identified as having comparative advantage, mainly energy and agricultural sectors.

> We are working with the authorities and with other development partners to improve the business environment to make sure we can make a dent in reducing economic informality and increasing favorable job creation. Strengthening governance and institutions will also help promote more inclusive economic growth.

Mr. Vasilyev noted that the press release included a sentence about the Debt Sustainability Analysis (DSA) that indicated that the risk of debt distress was assessed to be high because of the lagged effects of the deterioration of the institutional environment. He remarked that the sentence suggested a link between the deterioration of the institutional environment and the current risk of debt distress, but there was no economic link between those factors. There was only a statistical link. He suggested clarifying that the debt distress was assessed to be higher only due to methodology, not any changes in the economic situation.

Mr. Kiekens congratulated the staff for its strong work on the staff report, particularly with respect to the fiscal situation. Not only did the paper provide data for the economy as a whole, it also provided data for the non-extractive sector of the economy. He recommended a similar approach for all countries with a large or dominant extractive industry. This approach provided a better sense of how the economy was performing outside the extractive industry.

Mr. Daïri supported the comments made by Mr. Vasilyev about the reference to the DSA in the press release. The issue was clarified in the staff report, but the press release did not provide sufficient clarification about the methodology. He suggested removing the reference from the press release, given that readers who were interested in the DSA would be better served by reading the staff report itself.

The staff representative from the Middle East and Central Asia Department (Ms. Vera Martin) responded that the reclassification of the debt distress took into account the new methodology, but also the fact that economic conditions had changed compared the last Article IV consultation in 2012. The DSA reported an increase in external disbursements that had been incorporated in all projections. Consequently, it was not only the Country Policy and Institutional Assessment (CPIA) change in the methodology that resulted in the reclassification of debt distress.

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

> On the drafting, we can take another look to clarify the issue in line with the transparency policy. We will have to determine whether there is any ambiguity in it. But on the methodology itself, I would not say that it is purely

statistical. There is economic thinking behind the methodology. We use the three-year moving average precisely to avoid an adverse implication for the country of short-term changes in the CPIA, and the CPIA is a composite indicator of both institutional indicators and the economic policy making capability of the authorities. That is the methodology that is used for all of the eligible countries.

If we did not have this methodology, the risk rating would have been downgraded a few years ago. There has been as of late an improvement in the CPIA in Mauritania. The authorities have been taking steps to improve their institutional capacity. However, and unfortunately, this pace of improvement has not been fast enough to make up for the loss over the last few years.

Mr. Govil made the following statement:

I support the comments made by Mr. Vasilyev. There is a draft press release that will be issued. It says the risk of debt distress is assessed to be high because of X, Y, Z. Earlier, the risk of debt distress was assessed to be moderate. Something has changed this. I agree that many real things have also happened, the staff’s own paper on the DSA, in Supplement 2, states that the debt profile of the country has improved relative to the 2012 DSA because of X, Y, Z. Footnote 2 also states that it is because of the change in the CPIA rating. There may be a good reason for changing the methodology, nobody is arguing with that. The question is what has caused the change in the debt distress rating from moderate to high?

Footnote 2 makes it clear that if the current CPIA were used, Mauritania would have maintained the moderate risk of debt distress. We may have gone to an improved methodology, but the issue is that the change in the debt rating is only because of the change in methodology. To put it another way, if we had used this methodology earlier, then Mauritania would have been rated to be at a high risk of debt distress even earlier. That fine line has to be plotted out in the report, because otherwise it looks like that Mauritania has deteriorated in the last two years, which is not the case.

Mr. Daïri made the following statement:

The reference in this background section of the press release is confusing, because the reader would not understand why the deterioration would come from what happened in 2009, five years ago. Intuitively, if this is a moving average, and if we are using recent data, on the contrary, the 2009

> would be behind us, and it would show an improvement rather than deterioration.
>
> Why was 2009 included only now? Does this mean that the assessment the staff is using goes back to 2012 or 2011? If this is the case, yes. If the staff is talking about an average using 2009, 2010, 2011, whereas before the staff used earlier data that did not include 2009, then I would understand. But if the staff is using the years that go to 2012, 2013, or 2014, or at least 2011, 2012, 2013, there is no way that what happens in 2009 would affect the most recent assessment.

Mr. Alshathri saw merit in Mr. Govil's comments about Footnote 2, which suggested that Mauritania was deemed to have high debt distress because of methodological issues, not because there was an increase in debt. The first page of the report gave the impression that there would be an improvement in the debt level in the future, given expectations of bilateral debt relief and an increase in export-led growth, which would improve the debt level for Mauritania.

The staff representative from the Middle East and Central Asia Department (Ms. Vera Martin) responded that the DSA took into account developments on the debt, which had been increasing. The staff incorporated the average of the CPIA from 2011 to 2013, and while there had been an improvement in the institutional capacity, it had not been sufficient to provide for the country to have a higher debt tolerance level, as suggested by the methodology. She noted that the press release would be clarified to reflect that the staff expected a decline in the debt levels that hinged on reaching debt relief on the bilateral debt, and also on the fiscal consolidation path presented in the staff report.

Mr. Raghani made the following concluding statement:

> Our chair supports the comments made by Mr. Vasilyev, Mr. Daïri, Mr. Govil, and Mr. Alshathri.
>
> I thank Directors for their comments and recommendations, which I will convey faithfully to my authorities. I also thank management and the staff for the support to my Mauritanian authorities, and especially the mission chief, Ms. Vera Martin, for her dedicated work on Mauritania, which is much appreciated by the authorities. I also thank her for the answers to the questions raised by Directors.
>
> As Directors have noted, Mauritania has made considerable progress in recent years toward raising economic growth and achieving macroeconomic stability. However, this progress is being affected by the steep

decline in international prices of the main commodities exported, and the economic slowdown in key trading partners.

In this regard, I reiterate my authorities' commitment to continue implementing policies that maintain macroeconomic stability. They would also continue to have policies that promote growth and inclusiveness with a view to addressing the country's large social needs and providing employment opportunities, especially for the youth.

I have noted the emphasis placed by Directors on the following issues. First, in the fiscal area, many Directors have called for reforming the fiscal framework to address fiscal dependence on extractive resources, including through the introduction of a fiscal rule to help safeguard the budget against boom and bust cycles. My authorities believe that the implementation of a fiscal rule in a low-income country with considerable social needs like Mauritania would inevitably delay the implementation of the development agenda and ultimately weigh on the efforts to accelerate the fight against poverty. Nonetheless, they look forward to continued constructive discussions with the staff on the issue as a potential long-term reform.

Second, on monetary policy, Directors have recommended the strengthening of the monetary policy framework, including through the adoption of a formal liquidity forecasting framework, and the extension of the set of liquidity management tools. My authorities fully share Directors' views on the issue. In particular, they agree with the need to take advantage of the current low inflation environment to strengthen the monetary policy framework and reestablish the use of more direct and traditional liquidity management instruments, including interest rates and reserve requirements, and limit the use of indirect instruments, like foreign exchange intervention and treasury bills. They look forward to continued discussions with the staff on the formulization of monetary policy and the liquidity management framework.

As regards the external sector, my authorities agree with the assessment that in the context of declining reserves, a more flexible exchange rate would act as a shock absorber and the authorities intend to pursue efforts to further liberalize the foreign exchange market. However, given Mauritania's shallow foreign exchange market and other characteristics, including the considerably higher demand of foreign currency, they intend to pursue reforms in this area in a gradual manner.

Fourth, I have also taken note of Directors' emphasis on the need to accelerate economic diversification and promote more inclusive growth. My authorities have started to implement plans to increase the value added of production and diversification of the export base in areas where Mauritania has a comparative advantage, such as agriculture, livestock, and fishing.

Furthermore, they are promoting a private sector development strategy that is supported by an action plan to improve the business environment. The authorities have also taken steps to improve the business climate by eliminating minimum capital requirements and by introducing a one-stop shop to facilitate small- and medium-sized enterprise creation.

My authorities intend to continue to work closely with the Fund and other development partners to put in place the necessary policies to address the risks facing the economy, preserve the gains achieved, and continue the efforts to develop the economy.

The Acting Chair (Mr. Shinohara) noted that the Islamic Republic of Mauritania maintained exchange restrictions subject to Fund approval under Article VIII. The approval of those restrictions was recommended.

The following summing up was issued:

Executive Directors agreed with the thrust of the staff appraisal. They commended the Mauritanian authorities for policies that have secured macroeconomic stability and supported development in recent years. Directors noted, however, that the risks from further declines in iron ore prices and weak activity in key trading partners cloud the outlook for the near term. Accordingly, they encouraged the authorities to persevere with prudent policymaking and the implementation of institutional and structural reforms to boost the economy's resilience and foster more inclusive growth.

Directors welcomed progress with fiscal consolidation and the improved revenue performance. They agreed that the 2015 budget mitigates shortfalls in mining revenue, but considered that additional measures may be needed if the budget comes under pressure. Directors also stressed the importance of strengthening public financial management to reduce the risk of debt distress. Looking ahead, they underscored the need to improve the fiscal framework over the medium term to enhance the management of resource wealth and support macrostability. They recommended implementing an appropriate fiscal rule that takes into consideration the development needs of the country and helps safeguard the budget from boom-bust cycles of natural resource revenue, while reinforcing fiscal governance.

Directors encouraged the authorities to take advantage of the favorable inflation environment to reinforce Mauritania's monetary framework by strengthening liquidity management. They also noted that prompt recapitalization of the central bank is essential to safeguard its credibility and independence. Directors emphasized the importance of a gradual liberalization of the foreign exchange market, noting that greater exchange rate flexibility would help absorb external shocks and support the reconstitution of reserve buffers. They welcomed the authorities' steps toward compliance with Article VIII obligations, and encouraged them to eliminate the remaining exchange restriction as soon as possible.

Directors underscored the need to further strengthen the stability of the financial system. They welcomed the authorities' intention to implement the recommendations of the recent Financial System Stability Assessment. Priorities include strengthening regulatory enforcement and supervisory independence, expanding central bank supervision to cover public banks and the insurance sector, and enhancing the bank resolution framework.

Directors encouraged the authorities to accelerate reforms to promote private sector development and economic diversification, which would boost employment and reduce poverty. In particular, they recommended working closely with development partners to address infrastructure bottlenecks, invest in human capital and education, improve governance and institutions, and deepen financial inclusion.

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

The Executive Board took the following decision:

Islamic Republic of Mauritania—2014 Article VIII Consultation

1. The Islamic Republic of Mauritania maintains one exchange restriction subject to Fund jurisdiction under Article VIII, Section 2(a) of the Fund's Articles of Agreement arising from the insufficient availability of foreign exchange at the fixing sessions (auctions) organized by the Central Bank of Mauritania for those transactions that are required to be submitted to the fixing sessions.

2. In the circumstances of the Islamic Republic of Mauritania, the Fund grants approval of the retention of this exchange restriction until January 28, 2016 or the date of the conclusion of the next Article IV consultation, whichever is earlier. (SM/15/6, Supplement 3, 1/20/15)

Decision No. 15722-(15/9), adopted
January 28, 2015

APPROVAL: June 8, 2015

JIANHAI LIN
Secretary

Annex

The staff circulated the following written answers, in response to technical and factual questions from Executive Directors, prior to the Executive Board meeting:

Outlook/Risks

1. ***The current account deficit (CAD) is expected to remain around this level during the next few years; even if it is financed largely by relatively stable FDI inflows, the high level of CAD makes the economy highly vulnerable to foreign developments, which can be sources of instability. The staff is requested to comment on the authorities' plans to finance the CAD in the medium-term. Further, given the uncertainties surrounding the future commodity prices and the large import-burden created by FDI financed projects in Mauritania, we are skeptical about staff's projection that by 2021 the CAD would reach a long-term steady state figure of 6 percent. The staff's comments are welcome about the feasibility and risks associated with their long-term projection for CAD.***

- The projected current account deficit is predicated on mining investment taking place and being financed by FDI. The current account deficit would be much smaller if the investment plans were not to materialize.

- The staff currently projects that the planned mining expansion will go ahead under current iron ore prices projections, taking into account discussions with mining companies operating in Mauritania. The completion of investment projects will result in lower imports and higher exports, with the CAD projected to reach a long-term steady state level of 6 percent of GDP.

- Should iron ore prices decline further, expansion projects may be postponed and/or cancelled, resulting in a far lower long-run level of exports.

2. ***We would appreciate staff's assessment of the likely increase in the FDI related imports on account of such tripling of the iron ore output, and its impact on the external sector vulnerability. Does the economy have sufficient absorptive capacity that would allow it to make productive use of the likely FDI inflows?***

- The substantial rise in iron ore mining capacity in the country will require large investments over the medium run which will in turn necessitate sizeable annual imports as most of the materials for mine expansion are not produced domestically. The expansion will improve the long-run external position of the country but it will also increase other things equal, the external sector dependence global iron ore market developments. Such rise in production will therefore further increase the importance of diversifying the external sector away from reliance on mining exports.

- The mining expansion is undertaken by for-profit companies and, therefore, it is assumed that the related FDI will be used productively.

3. ***Given that the risk [of political and/or social unrest] is assessed as low, additional information on the indicators behind this assessment would be appreciated.***

- This assessment is based on the fact that President Abdelaziz has been recently reelected with a comfortable majority and that there are no major signs of political or social instability. In addition, the government commitment to undertake structural reforms for more sustainable and inclusive growth reduces the probability of political and social unrest in the near future.

4. ***Should the impact of the decline in iron ore price be mitigated by a higher decline in price of oil and food imports? We wonder if annualizing the current account deficit in the first half of 2014 is an informative indicator, given that oil prices took completely two different directions in the two halves of the year. Similarly, we wonder if the weakening in current account and decline in reserves in 2013 and first half of 2104 is actually reflecting the impact of high oil prices, and this should be reversed going forward once the impact of the recent decline in oil price starts to kick in.***

- The estimated 2014 current account deficit in the staff report considers both the developments in the iron ore and oil and food markets over the course of the full year. While lower oil and food prices have benefited the external sector of Mauritania, particularly in the second half of 2014, they have not been sufficient to compensate for the decline in iron ore prices and stem a decline in reserves, which have decreased by over 30 percent in nominal terms during 2014.

5. ***The large external financing gap estimates envisaged under the downside scenario with no mining expansion (box 2) do not seem to reflect that imports are dominated by capital goods that are tied to the mining activities and funded by FDI, which should help mitigate the impact of this shock on the external balance.***

- The estimates of developments under the downside scenario in Box 2 assume that delays and cancellations of mining projects result in concurrent decrease in FDI and capital goods imports.

6. ***In the context of the decline in commodity prices, do staff have information on a potential investments freeze in mining and hydrocarbons sector? Do you estimate the ambition to double mining production by 2020 achievable?***

- The baseline scenario already incorporates the information on recent project delays that is available to staff. The Banda-Gas project was postponed to unknown date after two foreign investors cancelled their participation to the project and was not incorporated into the baseline projections. Similarly, TASIAST delayed the expanding a gold mine in 2015 which was supposed to increase production by 2017. MCM stalled producing 1 million ton of iron ore in 2015.

- Under the baseline assumptions, we think that the ambition to double mining production by 2020 remains achievable owing to the fact that lower iron prices will be partially compensated by lower oil prices.

Fiscal Policy

7. ***Can the staff comment on the prospects for formal adoption of the Organic Budget Law, which has awaited approval since 2012?***

- The authorities intend to adopt the organic budget law in 2015; however its adoption could be delayed by the recent appointment of a new Minister of Finance. To gather support, the ministry of finance plans to organize workshops with line ministries in early 2015 to pave the way to its adoption. FAD technical assistance is planned to help the authorities implement the organic budget law.

8. ***How appropriate is the implementation of a fiscal rule in Mauritania given the current conditions?***

- The staff foresees the implementation of the fiscal rule as a medium-term objective to strengthen the conduct of fiscal policy. The staff considers that there are preconditions that need to be in place before moving ahead with implementing a fiscal rule. Moving ahead with the new organic budget law will help advance significantly with public financial management by revamping budget formulation and envisaging multi-year fiscal framework. A fiscal rule will also require building up capacity in the public administration and we plan to support the authorities with additional technical assistance.

9. ***Targeted social transfers to low-income households would help in employing government resources in a fiscally sustainable way. Could staff state the timeline for completion of the household survey being conducted for this purpose, the mechanism that would be used for transferring such subsidies to the poor households, and the scope of the project (i.e. what types of subsidies and what fraction of total subsidies would be targeted in this manner)?***

- The household survey is expected to be completed by mid-2015 and will serve, together with the 2013 population survey, to determine the registry of targeted households.

- The implementation of the targeted social transfers initially aims at covering the 100,000 poorest households in Mauritania, identified using the national identity number and to be included in the Social Registry. The beneficiary will be the person in charge of daily health and education of children, typically the mother.

- The program will be implemented under the oversight of the Steering Committee for the National Social Protection Strategy and associated Technical Committee and Social Protection Unit. The core activities of the national program would be implemented by the Agence Nationale Tadamoun. De-centralized and administrative structures will support implementation locally.

- It is expected that advancing with the implementation of the targeted social transfers will facilitate the dismantling of general subsidies (electricity and food, primarily).

10. ***We wonder how much space could be made available for an increase in education and health care expenditures. The staff's comments would be appreciated.***

- Health and education represent about 18 percent of the 2015 budgetary envelop (4.8 percent of GDP). To achieve decisive changes, bolder measures aimed at reducing general subsidies and improving the efficiency of the public investment could generate additional resources for health and education.

11. ***We would welcome staff's explanation on how a fiscal framework including a fiscal rule would affect the implementation of Mauritania's development agenda, which includes considerable economic and social infrastructure needs.***

- The staff views the fiscal rule as reinforcing macroeconomic stability by providing a sustainable and predictable path for the implementation of the country's development agenda. As illustrated by the selected issues paper, the fiscal rule will guide a level of public spending that is consistent with fiscal sustainability criteria, isolates spending from volatile resource revenues, and allows the smooth implementation of growth-supporting projects that are planned according to a medium-term expenditure framework. In the current context, staff views debt sustainability as the main consideration to provide room for critically needed spending to boost potential growth and eradicate poverty.

12. ***Could staff comment further on the contents of the Organic Budget Law under discussion in parliament and the prospects for it being passed the first half of 2015?***

- The organic budget law will update of the regulatory framework for public expenditure management. The key features of the law are inclusion of fiscal principles and setting of fiscal objectives under a medium-term budget framework with improved transparency and accountability. In addition, the law will allow for higher legislative scrutiny of the budget, and deadlines for in-year reporting of accounts and audit reports. The law will strengthen the normative framework for certain government operations including the use of immediate settlement requests, earmarked accounts, and emergency spending authorizations. The law will be applicable to central government, local governments, and public administrative institutions.

- The authorities are planning to have the draft law approved this year but the process could be delayed by the recent appointment of a new Minister of Finance.

13. ***We invite staff to elaborate on the type of fiscal rule that could serve Mauritania's needs to preserve fiscal sustainability while providing room for countercyclical response and critically needed spending to boost potential growth and eradicate poverty.***

- The specific design of the fiscal rule ultimately depends on an evaluation of the resource wealth horizon, the importance of resources in total budget revenues and country-specific conditions regarding the absorption capacity for public investment and inter-temporal preferences in managing non-renewable wealth. It is premature at this stage to provide specific recommendations, and the selected issues paper on this topic illustrates the options and decisions the authorities would need to consider.

14. ***Against the backdrop of lingering poverty, high unemployment rates, ageing population and rising inequalities, among other stalled social indicators, we wonder whether the current safety nets are sufficient to provide a good level of social protection. From staff's perspective, what additional measures, if any, could the authorities consider to overcome shortcomings in this area to improve living standards?***

- The authorities' efforts to implement targeted social transfers will provide better safety nets and improved living standards for the most vulnerable. Eliminating general subsidies (electricity and food) will provide resources for higher health and education expenditure to support human capital development and reduce the infrastructure gap. In addition, bolder structural reforms over the medium term aimed at improving overall productivity and creating the conditions for economic diversification will set the basis for job creation and opportunities to spur growth—ultimately promoting better living standards.

15. ***The staff recommends strengthening fiscal policy formulation to reduce reliance on mineral revenue, including through adoption of a fiscal rule and a fiscal anchor. However, the authorities are rightly concerned that such a framework could create unwelcome constraints on key social and infrastructure spending in a country with huge developmental needs. Could staff elaborate on how these reforms could be better adapted to a LIC environment?***

- The selected issues paper illustrates options for the fiscal rule to accommodate frontloading of public investment to support growth-enhancing programs, in line with the macroeconomic policy frameworks for resource-rich developing countries presented to the Board in 2012. Such investment will need to be planned and implemented taking into account existing capacity absorption and debt sustainability constraints. Given pressing development needs, scaling up domestic investment financed by natural resource wealth is likely to be part of an optimal strategy to generate lasting development gains.

Debt Sustainability

16. ***Could staff comment on the exposure to regional Arab lenders in light of the oil price drop?***

- The country's substantial share of outstanding external loans from Arab lenders is largely on concessional terms and at long maturity without the need to refinance in the short run, therefore the recent sharp oil price drop will not affect the country's external debt position.

17. ***Did staff consider available room for flexibility to avoid this downgrade for such a tiny shortfall? Could the use of borderline concept help address the issue? When is the earliest opportunity for updating the CPIA rating to take account of recent improvements in capacity?***

- The joint Bank-Fund debt sustainability framework unfortunately does not allow for flexibility in the use of CPIA scores in measuring a country's institutional capacity. The framework specifies detailed rules for translating a past history of CPIA scores into a country's institutional capacity classification. Mauritania's breach of a threshold in the baseline is too large to be considered borderline under the framework. CPIA scores are determined by the World Bank and a new score should be published in the summer of this year. Any formal DSA following that update would take into account the CPIA score published in 2015.

Monetary Policy

18. ***Could staff comment on the impact of further developments in this area in light of the announced European QE?***

- The announced European QE will impact Mauritania mostly through trade linkages as the capital account is not open other than for FDI. Under the current exchange rate regime (a stabilized exchange rate regime to the U.S. dollar), the European QE could lead to a real appreciation of the Ouguiya (an appreciation vis-à-vis the euro). This will lower inflation pressures but potentially lead to an acceleration of imports and a deterioration of the current account balance, calling for a more active monetary policy. The real appreciation of the Ouguiya will reduce Mauritania's external competitiveness vis-à-vis Europe, its second trading partner.

Financial Sector

19. ***Can the staff comment on the trade-offs that might be involved in their suggestion that the national development bank might serve as a primary bank to promote long-term credit, such as the benefits of longer-term funding for banks against the risk that this could inhibit the development of private funding markets?***

- Enhancing credit supply to the economy from private institutions is a priority for staff. To this end, the proposed FSSA roadmap aims to the soundness of the sector and enhance confidence so as to encourage the lengthening of the maturities of banks and microfinance funding beyond sight deposits, reduce information asymmetries and enhance the quality of the portfolio. As an alternative, however, the government created the CDD, a national development bank, which was envisaged to overcome some of the existing challenges and provide longer-term credit for projects banks would not be able to finance. But the institution requires first to be supervised as a bank, which is not yet the case.

20. *Could staff elaborate on the implementation capacity of the FSAP recommendations?*

- The FSSA recommendations and proposed timeline were designed taking into account the country's capacity constraints; technical support is expected to continue and support the designed work agenda, including by building up institutional capacity. Capacity is limited but efforts have been under way to reinforce central bank's ability to strengthen financial stability. In the past years, Mauritania has received significant TA support in the areas of supervision, monetary policy and foreign exchange markets. Moreover, an important focus of the TA has been on boosting implementation capacity, focusing on reinforcement of the supervision regulatory framework, off-site and on-site control methodologies and on banking supervision, training of the newly hired staff and reinforcement of the supervision regulatory framework, including supporting the operational independence of the BCM.

21. *We would appreciate more elaboration from staff on what measures are being considered to address the high level of NPLs, as well as the issue of the under-provisioning of some banks.*

- Until capacity is fully developed, the authorities' intention is to continue to undertake external independent audits of banks. At the same time, the newly hired and trained staff is expected to start conducting onsite supervision missions to banks throughout 2015. And the qualifications approval system by the BCM for auditors, based on objective and monitorable criteria, should help strengthen local auditing practices. Also, the BCM approved a new accounting regulation on credit operations in 2014, which should help accelerate the provisioning process of NPLs and the removal of some legacy, fully-provisioned unrecoverable debts from banks' balance sheets (a measure required by the IMF in the past).