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November 24, 1992

To: Members of the Executive Board

From: The Secretary

Subject: Cambodia - Overdue Financial Obligations to the Fund -
Review of Decisions to Limit Use of the Fund's General
Resources and Suspend Use of SDRs

The attached paper is proposed to be scheduled for consideration by the Executive Directors on Friday, December 11, 1992. A draft decision appears on pages 13 and 14.

Mr. Corr (ext. 38774) or Mr. Dodsworth (ext. 37091) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

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INTERNATIONAL MONETARY FUND

Cambodia - Overdue Financial Obligations to the Fund -
Review of Decisions to Limit Use of the Fund's
General Resources and Suspend Use of SDRs

Prepared by the Treasurer's, Central Asia, Legal
and Policy Development and Review Departments

Approved by David Williams, Hubert Neiss, François Gianviti,
and Thomas Leddy

November 23, 1992

I. Introduction

On December 19, 1978, the Executive Board limited Cambodia's access to the Fund's general resources and suspended its rights to use SDRs acquired after that date. 1/ These decisions resulted from the failure of Cambodia to fulfill certain of its obligations under the Articles of Agreement, including the accumulation of arrears in both the General and SDR Departments. Arrears had emerged in the General Department in March 1975 and in the SDR Department in April 1978. On December 19, 1978, Cambodia's arrears amounted to SDR 21.0 million, equivalent to 84 percent of its quota.

In view of the existence of arrears, the Executive Board decided on January 5, 1977 that the restitution of gold to Cambodia would be postponed until Cambodia had settled its outstanding financial obligations to the Fund. 2/ Similarly, the Executive Board decided that the distribution to developing country members of a percentage of the profits realized from the sale of the Fund's gold would not take place in Cambodia's case until Cambodia had settled these financial obligations. 3/ Consequently, the Fund holds on Cambodia's behalf 21,396 ounces of fine gold and US\$ 3,990,776 in undistributed Trust Fund profits. 4/

After the suspension of its right to use SDRs, Cambodia received allocations of SDRs in 1979, 1980, and 1981. The allocation in 1979 was used in part to settle the then overdue net SDR charges; Cambodia subsequently remained current in the SDR Department until November 1984, as the SDRs received in these allocations were used to pay net SDR charges and

1/ Executive Board Decisions No. 5990-(78/200) and 5989-(78/200)S, reproduced in Attachments I and II, respectively. Cambodia was at the time known as Democratic Kampuchea.

2/ Executive Board Decision No. 5312-(77/3), adopted January 5, 1977.

3/ Executive Board Decision No. 5710-78/41 TR, adopted March 23, 1978

4/ Cambodia did not receive any loans from the Trust Fund.

assessments. When the balance in its SDR account had fallen to zero, Cambodia once again became overdue in the SDR Department in November 1984 .

The Fund did not receive any replies to communications dispatched to Cambodia concerning its failure to comply with its obligations under the Articles of Agreement, including its overdue obligations. The Fund ceased to send communications after July 1979. Subsequently the Fund did not recognize any of the competing factions as the government of Cambodia. Because of the difficulty of resolving the issues of recognition and representation, the Fund did not take further action with respect to Cambodia and the matter of Cambodia's overdue financial obligations to the Fund has not been taken up in the context of the Fund's arrears strategy. Subsequent to the Paris Peace Accords of 1991, formal communications between the Fund and Cambodia were resumed in October 1992, following a finding by management that there existed in Cambodia a governmental structure with which the Fund could work. This finding became effective upon the provision by Cambodia of certain legal assurances, and the authorities' designation of a fiscal agency and depository. The Cambodian authorities are currently in the process of selecting a governor and alternate governor. 1/

In the meantime, an informal meeting of donors took place on September 23, 1992 at which it was agreed that a Support Group for Cambodia be established. At the meeting, several countries indicated their preparedness to provide financial contributions toward the clearance of Cambodia's arrears to the Fund in the context of the adoption of appropriate macroeconomic policies to be formulated with the assistance of the Fund staff. Accordingly, a mission visited Phnom Penh during October 14-28, 1992 to discuss steps toward the settlement of Cambodia's arrears and understandings were reached on a package of stabilization policies, the implementation of which will be informally monitored by the staff. 2/ In the period through the end of 1992, the authorities have agreed to implement the bulk of the fiscal measures, adhere to credit ceilings, and take specific actions in regard to interest and exchange rate policies. The policy package is discussed further in Section IV(d) below.

It is envisaged that, on this basis, a meeting of the Support Group for Cambodia will be convened before the end of 1992 to solicit pledges for the clearance of arrears. In this context, the Cambodian authorities have recently requested the Fund to utilize the assets it holds on behalf of Cambodia toward partial clearance of arrears. 3/ Looking beyond this, the authorities have also requested that Article IV consultation discussions

1/ See Statement by the Managing Director on Cambodia (BUFF/92/130, 10/21/92), in conjunction with Statement by the Staff Representative on Cambodia (EBD/92/213, 9/17/92).

2/ The Memorandum of Understandings is provided in Attachment III.

3/ See paragraph 3 of the letter of October 30, 1992 from the Cambodian authorities to the Managing Director (Attachment III). The authorities' request for the initiation of this process was received on November 18, 1992.

take place in January 1993. At that time, provided the necessary financing assurances are in place, including for the full clearance of Fund arrears, and policies are being implemented satisfactorily, the Article IV consultation mission would discuss the possible use of Fund resources with a view to negotiating a stand-by arrangement in the first credit tranche.

In light of these developments, it now appears appropriate for the Executive Board to consider the Fund's relationship with Cambodia in the context of a review of the decisions regarding suspension of the use of SDRs and limitation on the use of the Fund's general resources. This paper contains information for the Executive Directors' consideration at the review and proposes a course of action, including a draft decision. A companion paper on certain operational aspects of the Fund's financial relations with Cambodia is being issued for consideration by the Executive Board at the same meeting.

Section II of this paper covers developments with respect to Cambodia's arrears to the Fund. The matter of Cambodia's nonfulfillment of its nonfinancial obligations to the Fund is discussed in Section III. Section IV describes economic developments and policies in Cambodia in recent years, including the understandings reached with Fund staff on a macroeconomic policy program for the remainder of 1992 and 1993. The application of the Fund's strengthened arrears strategy in the case of Cambodia is discussed in Section V.

II. Overdue Financial Obligations

(a) Background

Cambodia's arrears in the General Department emerged in March 1975 and in the SDR Department in April 1978, and had reached SDR 21.0 million at the time of the limitation of Cambodia's use of the general resources and suspension of its right to use SDRs on December 19, 1978. On November 20, 1992, Cambodia's overdue financial obligations were SDR 43.5 million (Attachment IV), equal to 174 percent of Cambodia's quota and 232 percent of Fund credit outstanding to Cambodia. Of these arrears, SDR 18.7 million represent overdue principal, equivalent to 100 percent of Fund credit outstanding. Of Cambodia's overdue interest and charges of SDR 24.8 million, SDR 12.8 million comprise charges due to the General Resources Account (GRA), of which SDR 4.8 million represents deferred income.

As regards payments, since the adoption of the Executive Board decisions on December 19, 1978, Cambodia has made no payments to the Fund. In this period, Cambodia received SDR 7.08 million in newly allocated SDRs that was applied against Cambodia's obligations falling due to the Fund in the meantime.

The Fund holds certain assets on behalf of Cambodia, comprising 21,396 fine ounces of gold arising from the restitution of gold to members in the late 1970s and Cambodia's share of the profits of the Fund's earlier sale of

gold on behalf of developing country members. As noted below and elaborated in the companion paper, the authorities have requested the use of the assets held by the Fund on Cambodia's behalf (which together are valued at approximately SDR 8 million) in partial settlement of the overdue financial obligations.

The estimated total of forthcoming financial obligations of Cambodia through 1996 amounts to approximately SDR 6.8 million (Attachment V), ^{1/} consisting entirely of net SDR charges payable on the past allocations of SDRs received by Cambodia. Cambodia, which is current with the World Bank, is in the process of settling arrears of US\$ 2.1 million to the Asian Development Bank. Appendix Table 1 presents more information regarding Cambodia's debt service obligations and payments.

(b) General Department

Cambodia first became overdue on its financial obligations to the Fund in the General Department with respect to a Compensatory Financing Facility repurchase of SDR 6.25 million which was due on March 13, 1975. Subsequent to the occurrence of this overdue obligation, Cambodia failed to settle other repurchases and charges payable to the General Resources Account on a continuous basis, including a repurchase in respect of a gold tranche purchase made in September 1971. ^{2/} On November 17, 1978, at which time Cambodia's total arrears had reached SDR 20.8 million, a complaint of management under Rule K-1 was reported to the Executive Board. Cambodia was informed of the complaint and the Executive Board's intention to consider it; Cambodia failed to respond.

When a member fails to fulfill any of its financial obligations to the Fund in the General Department, the Fund may declare the member ineligible to use the general resources of the Fund, including reserve tranche purchases (Article XXVI, Section 2(a)). In 1978, the Executive Board decided not to pursue this course of action with respect to Cambodia. Rather, it decided in accordance with Rule K-2 of the Fund's Rules and Regulations, that Cambodia "may not make use of the general resources of the Fund until such time as Cambodia is fulfilling its obligations under the Articles of Agreement to which Article XXVI, Section 2(a) applies" (Attachment I).

^{1/} This projection assumes that Cambodia's overdue obligations to the Fund are settled by the end of 1992; to the extent that settlement is delayed much beyond that point, charges would be higher.

^{2/} On January 8, 1975 (EBM/75/2), the Executive Board agreed that repurchases in respect of the gold tranche purchase be made in six quarterly installments to be completed not later than August 20, 1976. Cambodia did not communicate with the Fund with respect to the Fund's schedule of repurchases in connection with its purchases under the Compensatory Financing Facility.

As the staff explained to the Executive Board at the time, the practical effects of this limitation on the use of the Fund's general resources are the same as that of a declaration of ineligibility. However, the Fund cannot proceed to compulsory withdrawal on the basis of a limitation under K-2, as it could after a declaration of ineligibility.

(c) SDR Department

Cambodia failed to observe its obligations in accordance with the reconstitution requirement in the financial quarter ending December 31, 1975, 1/ and also became overdue with respect to payment of assessments and net charges payable on the allocation of SDRs on April 30, 1978. If a participant in the SDR Department fails to fulfil obligations with respect to Special Drawing Rights in accordance with Article XX, Section 2 and 5, 2/ the Fund may suspend the right of the participant to use SDRs it acquires after the suspension (Article XXIII, Section 2(b)). The Executive Board adopted a decision to this effect on December 19, 1978 (Attachment II).

Subsequent to the suspension of its right to use SDRs, Cambodia received SDR 2.65 million during each of the second and third years of the third basic period of SDR allocations--1979 and 1980--and SDR 1.8 million during the fourth year--1981. These SDRs were deposited in Cambodia's SDR account, and Cambodia's overdue and subsequent obligations in the SDR Department, as well as assessment obligations in the General Resources Account, were settled automatically by debiting that account. Cambodia is now overdue with respect to charges in the SDR Department totaling SDR 12.0 million, the longest outstanding of which dates from November 1, 1984. The lifting of the suspension of Cambodia's use of SDRs, after Cambodia has become current in its obligations to the SDR Department, would require a decision of the Executive Board under Rule S-7.

III. Nonfulfillment of Nonfinancial Obligations

The nonfulfillment of obligations that has led to a limitation imposed by Decision No. 5990-(78/200) on the use of the Fund's general resources is not confined to financial obligations. This limitation will continue (unless otherwise modified or terminated by the Executive Board) until Cambodia has fulfilled all of its obligations under the Articles of Agreement, other than its obligations in the SDR Department.

1/ Under the reconstitution requirement of the Articles of Agreement prior to the Second Amendment, participants in the SDR Department were required to maintain minimum average daily balances over successive five-year periods (see Article XIX, Section 6, and Schedule G). This requirement was abrogated in April 1981.

2/ Under Rule T-1(a) the accounts of participants in the SDR Department are debited with the excess of charges over interest due.

With respect to Cambodia's fulfillment of its nonfinancial obligations, significant progress has been made. Specifically:

1. Although Cambodia has not yet notified the Fund of its exchange arrangements, as required under Article IV, Section 2(a) of the Articles, the staff expects that this notification will be received soon, at which time the staff will, as is customary, circulate this notification for the information of the Executive Board.

2. The Cambodian authorities have accepted the staff's proposal that a Fund mission arrive in Cambodia in January 1993 to hold the Article IV and Article XIV Consultation discussions. Accordingly, Cambodia will be complying with its obligations under Article IV, Section 3(b) and Article XIV, Section 3, once these discussions are under way.

3. If the Executive Board approves the representative rate for the Cambodian riel proposed in the EBS/92/ , the riel/U.S. dollar rate set forth in the letter from the Cambodian authorities dated October 28, 1992 will complete the procedure for determining the rate to be established under Article XIX, Section 7 (which is also to be utilized for purposes of an exchange of currency requested by the Fund under Article V, Section 3(e)(i) or Article V, Section 7(j)(i)). Further arrangements required for the exchange of currency are expected to be completed soon.

4. Cambodia failed to provide the monetary reserves data for the years 1975-1977 which would have enabled the Fund to calculate whether and when Cambodia's gold tranche and CFF purchases gave rise to a repurchase obligation under the pre-Second Amendment Article V, Section 7(b) (which, if accrued, would remain due pursuant to Schedule B, Section 1). However, Cambodia's failure to provide this information did not prevent a repurchase obligation with respect to these purchases from accruing pursuant to Schedule B, Section 4 (which applies to repurchase obligations that have not accrued under Schedule B, Section 1). Therefore, this information is no longer necessary for purposes of Schedule B, Section 1.

5. Of the minimum data required to be received from Cambodia under Article VIII, Section 5(a), the Fund has received information for the years 1988-1992. The staff expects to receive information for earlier years during the upcoming consultation discussions.

Limitations imposed under Rule K-2 are generally lifted automatically (i.e., without a further decision by the Executive Board) once the specified conditions have been met. In past cases, these conditions have normally been limited to the fulfillment of financial obligations. As has been discussed, however, the limitation imposed in the case of Cambodia also covers nonfinancial obligations, and a determination as to whether these obligations have been fully met will, in some instances, require the exercise of judgment, particularly with respect to the sufficiency of information to be provided under Article VIII, Section 5. Accordingly, if continued progress is made by Cambodia in the fulfillment of its nonfinancial obligations, the staff would propose, following Cambodia's

clearance of its arrears, that the Executive Board formally terminate the limitation imposed under Rule K-2.

IV. Economic Developments and Policies

(a) Developments to 1985

The catastrophic events in Cambodia in the 1970s--a lengthy civil war followed by the turmoil of 1975-79--reduced the country's population by over one million and eradicated virtually all aspects of a modern economy. Almost the entire workforce was harnessed to agriculture, industries were abandoned, and most of the physical and social infrastructure was destroyed. The banking system was dismantled and currency abolished; internal and foreign trade reverted primarily to a barter system.

By 1979, when the People's Republic of Kampuchea (PRK) was established, the country faced mass starvation with rice production estimated at only one fourth of its prewar level. The task of rehabilitation and reconstruction was initially helped by receipt of a relatively large amount of emergency humanitarian assistance from the international community. However, from 1982, when the period of emergency was declared over, the only remaining aid came from the former Soviet Union and other CMEA countries.

The PRK Government initially made considerable headway in rebuilding economic infrastructure and institutions. A central administration was re-established, the banking system was reopened, and a national currency reintroduced. Some factories were reassembled and fertilizer provided to farmers. This rebuilding took place, however, within a framework of a centrally planned system with most means of production placed under state ownership and direct control. In the absence of individual incentives, the recovery of output in both the agricultural and industrial sectors was slow. In the middle of the 1980s, production of most commodities remained well below the levels achieved in the late 1960s.

(b) The initiation of market-oriented reforms

The Government began a process of market-oriented restructuring in 1985. The private sector was officially recognized and joint ventures between the state and private sector were authorized. Most price controls were lifted with the exception of the prices of several key commodities including petroleum, electricity, cement, steel, and fertilizer. The reform process accelerated from 1989, in part to cope with the economic difficulties caused by a decline in Soviet aid and a worsening of the security situation. Property rights were restored and agricultural land began to be returned to the tiller. State-owned enterprises (SOEs) were granted considerable autonomy in their pricing and production decisions and a privatization program was initiated. In the same year, a decree on foreign investment was promulgated encouraging both joint ventures and wholly foreign-owned enterprises. In 1990, official exchange rates were

unified, and since then the official rate has shadowed the parallel market rate albeit with varying lags and differing spreads. 1/

Output initially responded briskly to the reforms in key agricultural sectors and small-scale private industries. By 1988, rice production regained its pre-1970 level, and the production of rubber recovered to about three quarters of the pre-1970 peak.

(c) Recent macroeconomic developments 2/

Following an output increase of 9-10 percent in 1988, economic growth slowed considerably in 1989-90 as a result of the unfavorable external factors mentioned above, particularly the decline in aid from the former Soviet Union. The consequent compression of imports led to a fall in industrial output, while the loss of budgetary receipts and the resulting monetization of the fiscal deficit led to rapid inflation which reached over 150 percent in 1990. Since then, some recovery in output has occurred reflecting a supply response to the acceleration of market reforms and increased confidence over the prospect of national reconciliation. In 1991, real GDP rose by 7-8 percent and a similar increase (6 1/2 percent) is expected in 1992. Inflation has continued to be high, however. The consumer price index rose by 82 percent during the year ending September 1992 and is expected to rise to over 200 percent by end-1992. 3/

The principal factor underlying the continuing inflation has been a deteriorating fiscal situation. 4/ The revenue-to-GDP ratio has declined owing to the inelasticity of the tax system and a decline in transfers from state enterprises, partly reflecting the loss of Soviet aid. While revenues are expected to partially recover to 5 percent of GDP in 1992, they have still to regain the level reached in 1989. At the same time, current expenditures, particularly outlays for military purposes, have grown rapidly. As a result, despite reductions in capital spending, the overall deficit has increased to an estimated 5 percent of GDP in 1992 from 2 3/4 percent of GDP in 1989. The financing of the fiscal deficit, which has been increasingly through money creation, has resulted in a threefold increase in domestic liquidity between end-1989 and end-1991, and a further 130 percent increase during the first nine months of 1992. As inflation has become more entrenched, the willingness to hold domestic currency has

1/ During the past two years, the spread between the official and parallel rates has averaged about 15 percent, and ranged from 4 percent to 37 percent.

2/ Key economic indicators are provided in Table 1 of Attachment III.

3/ The inflation rate at end-1992 is higher than the annual average for 1992 because of a sharp fall in the consumer price index in December 1991. The annual average inflation for 1992 is projected at 80-85 percent.

4/ Some additional pressure on prices in 1992 may have also resulted from the arrival and presence of the United Nations Transitional Authority in Cambodia which increased the demand for housing and some other domestically produced items.

declined significantly and substantial currency substitution has taken place. During the year ended September 1992, the riel depreciated against the U.S. dollar by 150 percent.

Cambodia's balance of payments is dominated by transit trade (more than half of recorded imports are re-exported, mainly to Viet Nam). However, exports (net of re-exports) have increased during 1991-92 largely as a result of higher production of timber and soybeans. Foreign inflows have also strengthened owing to higher private transfers, foreign direct investment, and services receipts associated with the United Nations' operations. The preliminary indications are that, after declining for three consecutive years, imports retained for domestic use will rise by about 25-30 percent in 1992. They will, however, still remain below the levels reached in 1988-89. Official reserves continue to be negligible at less than one week of retained imports. 1/

(d) Economic and Financial Policies for 1992-93

In collaboration with the Fund staff, the authorities have formulated and begun to implement a package of stabilization policies covering the remainder of 1992 and 1993. The understandings reached with the staff in October 1992 are set out in detail in Attachment III. The policy package is aimed at maintaining economic growth at 7-8 percent; reducing inflation to about 30 percent by the end of 1993; and increasing gross official reserves by about \$10 million during the course of 1993. To achieve these goals, the policies focus on fiscal adjustment, a move to positive real interest rates, and maintenance of a realistic official exchange rate. While the stabilization effort is under way, the authorities will continue to advance structural reforms toward a market-oriented economy.

The planned fiscal adjustment includes revenue measures which are estimated to raise an amount equivalent to 0.9 percent of GDP in 1993. These measures have begun to be implemented with the introduction of a hotel room tax (on October 16, 1992), and an upward revision of reference prices on which customs duties are based (on November 10, 1992). The customs price list has been adjusted to increase all riel-denominated prices by 20-60 percent and all U.S. dollar-denominated prices by at least 10-20 percent. At the same time, the basis for taxes on petroleum has been increased to reflect actual c.i.f. import prices. In addition, procedures have been put in place to ensure that all importers pay full customs duties prior to customs clearance. Supplementing these actions, steps are to be taken by January 15, 1993, to further strengthen revenues from customs duties and to raise taxes on petroleum products. The authorities also intend to implement

1/ Gross official reserves are defined as holdings by the National Bank of Cambodia. Inclusion of foreign exchange holdings of the state-owned Foreign Trade Bank would raise the level of gross reserves to \$18 million (1 1/2 months of imports) at end-June 1992. At that date, net official reserves using the latter concept were minus \$30 million.

measures to improve tax administration, and Fund technical assistance is expected to be provided in this area.

The 1993 budget will incorporate a reduction in current expenditures of about 1 percent of GDP based on a restrained wage policy and lower military and security expenditures in proportion to GDP. 1/ The reduction in military outlays reflects mainly a reversal of the overruns that occurred in 1992 and would be facilitated by the exercise of effective control by UNTAC personnel. 2/ Capital expenditures, on the other hand, are expected to rise from less than 1 percent of GDP in 1992 to 3 percent of GDP in 1993 as donor-financed projects come on stream. Given the indications from donors as to the extent of commodity assistance, it is envisaged that the amount of bank financing of the budget required for 1993 as a whole would be less than 0.2 percent of GDP.

With this as background, the monetary program for 1993 aims to slow the growth of domestic liquidity to about 30 percent, compared with an estimated 170 percent in 1992. Monetary policy is still at an early stage of development, and the authorities accordingly will need to rely initially on bank-specific credit ceilings and Ministry of Finance directives to ensure adherence to the credit program. Planned credit policies through end-1993 (as set out in Table 2 of Attachment III) incorporate a significant increase in private sector credit, but continue the restrictive policies the authorities have been implementing in regard to public enterprises.

The banking system is still undeveloped and is largely "dollarized" in its deposit and lending operations. Much of the financial intermediation and foreign exchange transactions takes place in parallel markets. In order to attract domestic currency deposits into the commercial banks and to encourage foreign exchange dealings to take place through legal channels, the authorities intend to: (i) raise interest rates on riel-denominated assets and liabilities toward levels that are positive in real terms; and (ii) set the official exchange rate close to the parallel market rate with a view to the ultimate unification of exchange rates. Specifically, from December 1, 1992, banks will be allowed to raise interest rates for riel deposits initially to 6 percent per month and will be allowed to determine their own lending rates. In addition, the official exchange rate will, from end-October, be set in a flexible manner so as to ensure that the differential between the official and parallel market rates will be limited to 5

1/ In response to a request from the authorities, a staff mission is expected to visit Phnom Penh during November 30 - December 10, 1992 to assist in the formulation of the 1993 budget.

2/ Reflecting the latest political developments, including the nonparticipation of Khmer Rouge forces in the demobilization process, the cut in military outlays incorporates a delay in timing and a reduction in the number of troops to be demobilized compared with that envisaged in the Paris Peace Accords. In the event of an escalation of the internal conflict, these savings may be difficult to achieve, in which event, alternative fiscal adjustment measures would be called for.

percent. At the end of October 1992, the official exchange rate was CR 2000 per US dollar, while the parallel rate was at CR 2100 per US dollar.

The authorities will also continue to implement structural reforms to develop a market economy. Further progress is expected in the privatization of state-owned enterprises (SOEs) and the autonomy of SOEs that remain under direct state ownership will also be strengthened. Private sector involvement in the provision of inputs for agriculture will continue to be encouraged and remaining public sector subsidies will be phased out. In the financial sector, the development of a two-tier banking system will be continued and steps will be taken to strengthen the central bank's supervision capabilities.

(e) External assistance requirements

As indicated in Section IV of Attachment III, to meet the level of imports required for the achievement of the goals set for 1993, donor assistance of about \$135 million will be needed in the forms of commodity and project aid. For 1994-96, to sustain output growth of 7-8 percent per year, the annual requirement for concessional assistance would remain in the range of \$130-140 million. At a Ministerial Conference held in Tokyo in June 1992, bilateral and multilateral donors expressed strong support for Cambodia, pledging \$880 million to be disbursed over the coming 2-3 years. Bilateral donors are presently translating these pledges into project and commodity assistance programs. As regards multilateral institutions, the Board of the Asian Development Bank (AsDB) will consider on November 26, 1992 a Special Rehabilitation Assistance Loan (amounting to about \$68 million). In addition, the World Bank is at an advanced stage of preparation of an Emergency Rehabilitation Credit, which will be negotiated in January 1993.

In addition to the clearance of arrears to the Fund, debt relief will be required in order to regularize Cambodia's debt service obligations and arrears to official bilateral creditors. Efforts are underway with regard to the quantification of these obligations and, as information becomes available, the authorities are initiating the contacts with the bilateral creditors, including through the Support Group, on an appropriate treatment of these obligations.

As for technical assistance, a number of projects are under preparation, including a comprehensive program on macroeconomic management jointly administered by the AsDB, UNDP and the Fund. A series of Fund missions have already visited Phnom Penh following the signing of Paris Accords in October 1991 to provide policy and technical advice to the authorities (Attachment VI). In view of the considerable need for institution rebuilding, further assistance from the international community will be required for some time, taking into account the absorptive capacity of the authorities for new ideas and processes.

V. Application of the Strengthened Arrears Strategy

The situation with respect to Cambodia may be summarized as follows. Cambodia has been in arrears to the Fund continuously since March 13, 1975. From December 19, 1978--when the Fund decided to limit Cambodia's use of Fund's resources and to suspend its use of SDRs--until recently, the Fund was not in a position to take further action to address the issue of overdue obligations of Cambodia. Thus, the timetable of procedures with respect to overdue financial obligations which has been developed in the course of elaboration of the Fund's arrears strategy has not been applied in the case of Cambodia. Under the timetable agreed in March 1990, a review following a decision on limitation, with a possibility of a second review if warranted, would normally take place to enable the Executive Board to evaluate the circumstances of the member and to arrive at a judgment regarding the appropriate response by the Fund including, if necessary, a declaration of ineligibility.

Such reviews would normally take place 6-12 months after the emergence of arrears and before a declaration of ineligibility is issued. Notwithstanding the considerable time that has lapsed since the adoption of the decision on limitation in the case of Cambodia, the staff proposes that, in light of the lengthy absence of communication between the Fund and Cambodia, the timing of any further steps under the strengthened arrears strategy be considered in relation to the date of re-establishment of relations with Cambodia rather than in relation to the date of emergence of arrears. In considering what further steps might be appropriate, the staff would, in accordance with the arrears strategy, be guided by the Executive Board's assessment of the specific circumstances of Cambodia and of the efforts being made by the member to fulfill its overdue financial obligations to the Fund.

As noted above, Cambodia has requested the Fund to apply Cambodia's assets held by the Fund (which amount to approximately SDR 8.0 million, equivalent to about 18 percent of the arrears) to the partial settlement of its overdue obligations. The decisions necessary to implement this request are proposed in the companion paper. The authorities have also indicated the importance they attach to the full clearance of arrears to the Fund as soon as possible, and with the assistance of the Support Group established for Cambodia, it is possible that clearance could take place early in 1993.

It is also encouraging that the authorities have formulated and begun to implement economic adjustment policies, as described above and set out in Attachment III. The macroeconomic policy package, to be informally monitored by the Fund staff, will serve as a basis for mobilizing donor assistance. The staff is tentatively scheduled to return to Phnom Penh in early December 1992 to assist in the formulation of the 1993 budget, and again in early 1993 to conduct the Article IV and Article XIV consultation discussions with the Cambodian authorities.

In view of the progress to date, including the prospect of early clearance of the arrears and the steps toward fulfillment of Cambodia's

nonfinancial obligations to the Fund, the staff does not propose that the Executive Board consider remedial measures in the case of Cambodia at this time. The staff's suggested course of action is set out in the draft decision below.

The draft decision, *inter alia*, welcomes the progress toward the normalization of relations with Cambodia, and the authorities' request to apply the assets held by the Fund to partial settlement of the arrears, and calls on the membership to cooperate fully in the implementation of the intensified collaborative approach so as to facilitate the prompt and full clearance of Cambodia's overdue obligations to the Fund. In light of the planned staff mission to Cambodia in early 1993 to conduct discussions for the 1993 Article IV and Article XIV consultation, it is proposed that the Fund review again the matter of Cambodia's nonfulfillment of its obligations to the Fund at the time of the Executive Board's consideration of the report for the 1993 Article IV consultation, and in any event within four months, if the overdue obligations have not been settled in the meantime.

Accordingly, the following draft decision, which could be adopted by a majority of the votes cast, is proposed for adoption by the Executive Board:

Draft Decision

1. The Fund has reviewed Decision No. 5990-(78/200) and Decision No. 5989(78/200)S in light of the facts and developments described in EBS/92/188 (11/24/92).
2. The Fund welcomes the progress toward the normalization of relations with Cambodia. The Fund further welcomes the authorities' adoption of macroeconomic adjustment policies aimed at sustained economic growth, financial stability, and balance of payments viability, and the progress Cambodia has made toward fulfilling its nonfinancial obligations to the Fund. The Fund intends to collaborate actively with Cambodia in this effort and stands ready to assist Cambodia in any appropriate way.
3. The Fund welcomes Cambodia's request that the Fund apply the assets held by the Fund on its behalf toward partial settlement of Cambodia's overdue financial obligations. Nevertheless, the Fund regrets the continued existence of Cambodia's arrears to the Fund, which places a financial burden upon other members and reduces Fund resources available to help others. The Fund stresses that full settlement of arrears to the Fund should be given the highest priority and notes that steps toward their settlement are being taken. The Fund calls on the membership to cooperate fully in the implementation of the intensified collaborative approach so as to facilitate the prompt and full clearance of Cambodia's overdue financial obligations to the Fund.

4. The Fund will review the matter of Cambodia's nonfulfillment of its obligations to the Fund again at the time of the Executive Board's consideration of the report for the 1993 Article IV consultation with Cambodia, and in any event within four months from the date of this decision, in the light of actions taken by Cambodia in the meantime to fulfill its obligations, including the settlement of its arrears to the Fund, and to implement a comprehensive adjustment program.

Attachments

INTERNATIONAL MONETARY FUND

Cambodia - Overdue Financial Obligations -
Complaint Under Rule K-1

Executive Board Decision No. 5990-(78/200)
Adopted December 19, 1978

Limitation of Right to use General Resources

1. The Managing Director has reported under Rule K-1 of the Fund's Rules and Regulations to the Executive Board the facts on the basis of which it appeared to him at the dates of these reports that Democratic Kampuchea was not fulfilling its obligations under the Articles of Agreement. These facts have been communicated to the authorities of Democratic Kampuchea.

2. On November 17, 1978, the Managing Director filed the following complaint in accordance with Rule K-1:

It appears to me that as of November 1, 1978, Democratic Kampuchea is not fulfilling the following obligations under the Articles of Agreement other than obligations referred to in Rule K-1:

(a) to repurchase SDR 18,743,538, including a repurchase of SDR 6,243,538 in respect of a gold tranche purchase made in September 1971, and repurchases in respect of two purchases totaling SDR 12,500,000 made in March 1972 and April 1973 under the compensatory financing facility, under Schedule B, paragraph 4.

(b) to pay charges of SDR 2,260,533 under Article V, Section 8(b) and (c).

(c) to notify exchange arrangements under Article IV, Section 2(a).

(d) to consult under Article IV, Section 3(b), and under Article XIV, Section 3, since 1973.

(e) to make arrangements for the exchange of currency of Democratic Kampuchea under Article V, Section 3(e)(i), and Article V, Section 7(j)(i).

(f) to provide monetary reserves data for the last three financial years ended before the entry into effect of the Second Amendment (financial years ended April 30, 1975, 1976, and 1977) under Article VIII, Section 5, and Schedule B, paragraph 1. This information is necessary for the calculation of repurchase obligations for these financial years under Article V, Section 7(b), before

the Second Amendment, which are to be discharged under Schedule B, paragraph 1.

(g) to provide information for the last four years under Article VIII, Section 5.

(h) to consult on the procedure for determining rates of exchange for the member's currency under Article XIX, Section 7(c).

3. In accordance with the decision of the Executive Board, the Managing Director informed Democratic Kampuchea:

- (i) that the complaint set forth in paragraph 2 above had been placed on the agenda for consideration by the Executive Board at a meeting to be held on December 19, 1978; and
- (ii) that Democratic Kampuchea had the right, under the Articles and By-Laws, to present its views both orally and in writing through an appropriately authorized representative at the meeting of the Executive Board on December 19, 1978, and at such subsequent meetings as the Board might hold on the matter.

4. The Government of Democratic Kampuchea has not availed itself of the opportunity mentioned in the Managing Director's cable.

5. After careful consideration of the complaint and the reports of the Managing Director, the Fund finds that Democratic Kampuchea has failed to fulfill its obligations under the Articles of Agreement as stated in the complaint filed by the Managing Director on November 17, 1978 and as set out in paragraph 2 above.

6. In view of paragraph 5 above, the Fund has a choice of actions to protect the general resources of the Fund and the interests of its members. It is authorized to declare Democratic Kampuchea ineligible to use the general resources of the Fund or to refrain from a declaration of ineligibility and to adopt the lesser course, in accordance with Rule K-2 of the Fund's Rules and Regulations, of deciding that Democratic Kampuchea may not make use of the general resources of the Fund until such time as Democratic Kampuchea is fulfilling its obligations under the Articles of Agreement to which Article XXVI, Section 2(a), applies. The Fund decides to adopt the action under Rule K-2.

INTERNATIONAL MONETARY FUND

Cambodia - Overdue Financial Obligations -
Complaint Under Rule S-1

Executive Board Decision No. 5989-(78/200) S
Adopted December 19, 1978

Suspension of Use of SDRs

1. The Managing Director has reported under Rule S-1 of the Fund's Rules and Regulations to the Executive Board the facts on the basis of which it appeared to him at the dates of these reports that Democratic Kampuchea was not fulfilling its obligations under the Articles of Agreement with respect to special drawing rights. These facts have been communicated to the authorities of Democratic Kampuchea.

2. On November 17, 1978, the Managing director filed the following complaint in accordance with Rule S-1:

It appears to me that as of November 1, 1978, Democratic Kampuchea is not fulfilling the following obligations under the Articles of Agreement that are referred to in Rule S-1:

(a) to meet the requirements of reconstitution under Article XIX, Section 6, and Schedule G of each of 12 successive reconstitution periods, the latest of which ended September 30, 1978.

(b) to pay charges of SDR 290,144 under Article XX, Section 2.

3. In accordance with decisions of the Executive Board, the Managing Director informed Democratic Kampuchea:

(i) that the complaint set forth in paragraph 2 above had been placed on the agenda for consideration by the Executive Board at a meeting to be held on December 7, 1978, and that consideration of the complaint had been postponed until December 19, 1978; and

(ii) that Democratic Kampuchea had the right, under the Articles and By-Laws, to present its view both orally and in writing through an appropriately authorized representative at the meetings of the Executive Board on December 7, 1978, on December 19, 1978, and at such subsequent meetings as the Executive Board might hold on the matter.

4. The Government of Democratic Kampuchea has not availed itself of the opportunities mentioned in the Managing Director's cables.

5. After careful consideration of the complaint and the reports of the Managing Director, the Fund finds that Democratic Kampuchea has failed to fulfill its obligations under the Articles of Agreement as stated in the complaint filed by the Managing Director on November 17, 1978 and as set out in paragraph 2 above.

6. In view of paragraph 5 above, the Fund, acting under Article XXIII, Section 2(b), suspends the right of Democratic Kampuchea to use special drawing rights it acquires after the date of this decision.

Phnom Penh, Cambodia
October 30, 1992

Dear Mr. Camdessus,

At a meeting on September 22, 1992, the Supreme National Council affirmed its intention to normalize Cambodia's relations with the International Monetary Fund. To this end, the National Bank of Cambodia was designated as fiscal agency and depository for Cambodia in its financial relations with the IMF, and the Supreme National Council and the United Nations Transitional Authority in Cambodia (UNTAC) provided the necessary legal assurances.

As you are aware, the key step to full normalization of relations is the clearance of Cambodia's overdue obligations to the IMF which presently stand at SDR 43 million. Several donor countries have indicated their willingness to assist in the clearance of these arrears, and a Support Group for this purpose, co-chaired by the Japanese and French authorities, has been established.

A meeting of the Support Group is expected to be convened before the end of 1992. At that meeting, donors will consider the policies being adopted to stabilize economic conditions in Cambodia and are expected to make pledges toward the clearance of IMF arrears. In regard to economic policies, there have been discussions with IMF staff and understandings have been reached on a stabilization program for Cambodia which is being implemented by the Administration of the State of Cambodia Party as described in the Memorandum of Understandings on Economic and Financial Policies for 1992-93. In regard to arrears, it is intended that the assets currently held by the IMF on behalf of Cambodia (totalling about SDR 8 million) would be utilized in partial payment of the overdue obligations to the IMF. An appropriate request for the initiation of this process will be sent to you shortly by the National Bank of Cambodia. The Supreme National Council will also request the cancellation of existing official debts to bilateral creditors. It is envisaged that requests for cancellation would be made, in part, in the context of the forthcoming Support Group meeting. While the requests are under consideration, an effective deferment of payments from all official bilateral creditors will be sought.

We are hopeful that the necessary external assistance to clear the IMF arrears as well as assurances in regard to overdue obligations to official bilateral creditors would be forthcoming at the Support Group meeting. Thereafter, we would wish to proceed as speedily as possible toward full normalization of relations with the IMF. We would suggest that discussions for an Article IV consultation could take place in January 1993. At that time, provided the necessary financing assurances are satisfactorily in place and economic policies are being implemented as indicated in the Memorandum of Understandings, we would wish to discuss with the IMF staff the possible use of Fund resources with a view to requesting a stand-by arrangement in the first credit tranche.

Your support at this critical time for Cambodia is highly appreciated.

Please be assured of our highest consideration.

/s/

/s/

Samdech Preah Norodom Sihanouk
Chief of State
President
Supreme National Council

Yasushi Akashi
Special Representative of
the Secretary General
United Nations Transitional
Authority in Cambodia

Mr. Michel Camdessus
Managing Director
International Monetary Fund
700 19th Street, N.W.
Washington, D.C. 20431

CONFIDENTIAL

**Memorandum of Understandings on
Economic and Financial Policies for 1992-93**

Phnom Penh, Cambodia
October 28, 1992

I. Introduction

Despite a surge in economic activity over the past two years, the Cambodian economy faces severe macroeconomic problems resulting from high inflation, a large budget deficit, and insufficient foreign exchange. It is recognized that, in order to maintain the recently established growth momentum, these problems need to be addressed on an urgent basis.

This memorandum reflects the understandings reached with the visiting IMF mission on policies to tackle Cambodia's pressing economic problems. The policy package that is to be implemented during the remainder of 1992 and in 1993 is aimed at sustaining economic growth, substantially lowering inflation, and strengthening the external position. The main thrust of the policies is to significantly reduce the deficit on current transactions of the budget by revenue enhancement and expenditure reduction measures, in order to limit, and eventually eliminate, the need for budgetary bank financing. Complementing the fiscal adjustment, monetary policy will be tightened through restraint on bank credit and through an increase in interest rates toward positive real levels. The official exchange rate will be managed in a flexible manner and will be kept close to the parallel market rate. While these policies are under way, the authorities will continue to advance and improve the market-oriented reform process which began in 1989.

II. Stabilization Policies for 1992-93

1. Policy objectives

On the basis of the policies outlined in this memorandum and expected external financing, the objectives for 1993 are as follows: (i) to increase real GDP growth to 7-8 percent from 6.5 percent in 1992; (ii) to reduce consumer price inflation (measured over 12 months) to 30 percent by end-1993 from an estimated 210 percent at end-1992; and (iii) to increase gross official reserves during 1993 by about \$10 million. The achievement of these objectives will depend not only on the prompt implementation of the measures described below, but also on the provision of necessary financial support from the donor community and from Cambodia's creditors. The external assistance requirements of the program and the proposed debt strategy are set out in section IV below.

2. Fiscal policies

The planned reduction in inflation will depend critically on corrective actions to strengthen fiscal revenues and limit the growth of current expenditures. The principal budgetary targets are as follows: (i) to increase the revenue-to-GDP ratio from about 4 1/2 percent in 1991 to over 5 percent in 1992 and to about 5 1/2 percent in 1993; (ii) to limit current expenditures to 9 3/4 percent of GDP in 1992 and to reduce these to 8 3/4 percent of GDP in 1993; (iii) to increase capital spending in line with available external project assistance and absorptive capacity; and (iv) to limit bank financing of the budget to CR 35 billion during October-December 1992 and to CR 10 billion during 1993.

a. Strengthening budgetary revenues

Revenue efforts have begun with the introduction of a hotel tax on October 16, 1992 which is expected to increase budget revenues by CR 0.7 billion in 1992 and CR 8 billion (0.15 percent of projected GDP) in 1993. This measure will be supplemented by several actions to improve customs collections. By November 15, 1992, the Customs valuation price lists will be revised to increase all riel-denominated prices by 20-60 percent and all U.S. dollar denominated prices by at least 10-20 percent. In addition to valuations which more accurately reflect import prices, procedures will immediately be put in place to ensure that all importers pay the full customs duty prior to customs clearance, and measures will be adopted to deter smuggling. The initial impact on customs revenue (excluding petroleum duties) is estimated at CR 1.3 billion per month (about 20 percent of average monthly receipts from this source). However, without more regular adjustments, the increase in revenues in real terms would soon be eroded by inflation. To avoid the need for recurrent revisions of the customs price list, an invoice system of valuation will be introduced by January 15, 1993. Initially, the invoice system will be used in combination with the price list system. However, by January 15, 1993 all prices under the price list system will be denominated in U.S. dollar equivalents. The above measures to improve customs collections, taken together, are expected to raise budgetary revenues by CR 30 billion (0.6 percent of GDP) in 1993.

Measures will also be taken to increase the taxation of petroleum products. By November 15, 1992, the customs valuation of petroleum products will be revised to reflect actual c.i.f. prices, and customs valuations will thereafter be denominated in U.S. dollar equivalents. List prices would be raised, for instance, for gasoline and diesel from \$0.10 per liter to about \$0.17 per liter. ^{1/} Procedures will also be put in place to ensure that all petroleum products, whether imported by the public or private sector, will be subject to the full customs duty, with payments made prior to customs clearance. It is estimated that these changes will result in an

^{1/} To minimize the impact on poorer households, kerosene would not be included in these changes.

increase in revenue of CR 2 billion (about 0.05 percent of GDP) in 1993. Supplementing these measures, by January 15, 1993 (following the National Assembly's decision to amend the Import and Export Goods Taxation Law) the rate of customs duty on gasoline and diesel will be raised from 5 percent to 10 percent, resulting in a further increase in budgetary revenue of CR 4 billion (0.1 percent of GDP) in 1993.

The combined impact of the introduction of the hotel tax, increased customs collections, and higher petroleum taxation is estimated at 0.85 percent of GDP in 1993. In addition, improvements will be made in the administration of the turnover and other taxes, so as to expand the domestic tax base and spread the tax burden more equitably. Efforts have already begun to rationalize the tax administration machinery and improve the accuracy of assessment of the turnover and profits of enterprises.

b. Controlling budgetary spending

The planned reduction in current expenditure by 1 percent of GDP in 1993 is expected to result mainly from a restrained wage policy and a lower level of military and security expenditures in proportion to GDP. While it is recognized that real wages of civil servants have declined over the past two years, there is limited scope for recouping the entire loss in 1993. The increase in public sector wages is nevertheless targeted at 85 percent--reflecting the projected average increase in prices between 1992 and 1993. Savings in military outlays will depend, in part, on the progress in demobilization of forces from all factions in Cambodia. However, it is expected that budgetary military and security expenditures could be limited to CR 175 billion (3.4 percent of GDP) in 1993. On the basis of projected aid, capital expenditures would rise from less than 1 percent of GDP in 1992 to 3 percent of GDP in 1993 as donor-financed projects begin to come on stream. Public investment, however, will be tailored to the availability of external assistance.

The use of bank financing of the budget will depend, in part, on the extent of external commodity assistance. Additional commodity assistance at an early stage--in the last quarter of 1992 and the first quarter of 1993--would be helpful in reducing reliance on bank financing and inflationary pressures. Recent indications from donors suggest that the amount of bank financing required for 1993 as a whole would be small--less than 0.2 percent of GDP. However, the credit requirements of the budget would remain relatively high in the first quarter of 1993. Only during the second half of the year would inflows of commodity aid help to reduce the net credit from the banking system. The quarterly phasing of net credit for the budget is given in Table 2 attached to this Memorandum. It is recognized, as indicated in Table 2, that additional bank financing may be needed if external assistance is delayed or does not materialize.

3. Monetary policies

The monetary program for 1993 will aim to slow the growth of domestic liquidity to 30 percent compared with a projected 170 percent in 1992. To

help meet this target, the National Bank of Cambodia will closely monitor bank lending and implement necessary measures, including bank-specific ceilings, to contain net domestic assets of the banking system within the quarterly targets indicated in Table 2. Reflecting its present low level, private sector credit is expected to increase by about 25 percent in real terms during 1993. Credit to public enterprises, however, will be maintained at about the same level in nominal terms as in 1992.

To encourage people to hold riel liquidity in the form of bank deposits rather than in currency, the National Bank of Cambodia will, from December 1, 1992, allow banks to offer three-month term deposits at a minimum interest rate of 6 percent per month. From that date, the banks will be allowed to set their own interest rates on riel-denominated loans, and interest on commercial bank deposits with the National Bank will be paid at a 0.25 percentage point premium over the three-month deposit rate. If there are initial losses incurred by the National Bank from this scheme, these would be covered by a budgetary allocation. Following the introduction of the new system, the National Bank will, as appropriate, adjust the minimum deposit rate to reflect changes in the underlying rate of inflation. It is envisaged that the interest rate would decline steadily during 1993.

4. Exchange rate policy

The National Bank of Cambodia will continue to operate a flexible policy with regard to the official exchange rate. The ultimate goal is to have a relatively stable exchange rate, supported by strong fiscal and monetary policies. However, until there are sufficiently tight financial policies in place and domestic inflation is brought under control, the exchange rate would be expected to depreciate though at a less rapid pace than in the past year. In setting the official exchange rate, the National Bank of Cambodia will take into account the overall balance of payments position and movements in the parallel market exchange rate. To encourage flows of foreign exchange into the banking system, the differential between the official rate and the parallel market rate would be contained within 5 percent.

III. Structural Reforms

To further the development of a market economy, the implementation of structural reforms will continue. Progress will be made in the privatization of state-owned enterprises (SOEs), and the process of privatization will be rationalized, with special attention being given to proper valuation of assets and the supervision of lease contracts. The policy of financial and managerial autonomy for the SOEs that remain under direct state ownership will also be strengthened. More effective supervision and regulation of both leased and autonomous enterprises will be facilitated by development of a new accounting code and regulations.

In agriculture, private sector involvement in the provision of inputs will continue to be encouraged and remaining public sector subsidies will be phased out. Institutional reforms will be aimed at the development of rural financial services, to expand credit to farmers and help mobilize rural savings. To establish a modern banking system which is suitable for a market economy, the development of a two-tier system will be continued and steps will be taken to strengthen the National Bank's supervision capabilities.

IV. External Assistance Requirements and Proposed Debt Strategy

The projected external financing requirements for 1993-96 (Table 3) take into account the following: (i) import requirements to sustain output growth at 7-8 percent per year; (ii) the need to promptly regularize financial relations with multilateral and bilateral creditors; and (iii) the need to raise official reserves from present low levels.

A substantial increase in imports will be required over the coming years, inter alia, to slacken input constraints on production and to allow the rehabilitation of badly-depleted public services and infrastructure. For 1993, retained imports are estimated to increase by about 90 percent, largely reflecting higher project and commodity assistance. To cover the import requirements for 1993, donor assistance is estimated at \$76 million in the form of commodity aid and \$57 million in project aid. For 1994-96, with import growth projected at 10-12 percent per year, the annual requirement for concessional assistance would remain in the region of \$130-140 million.

The clearance of Cambodia's arrears to the Fund is expected to entail: (i) the use of assets currently held by the Fund on behalf of Cambodia (totalling SDR 7.8 million); (ii) financial contributions from donors (estimated at a minimum of SDR 30.3 million); and (iii) the use, by means of a bridging facility, of part of Cambodia's reserve tranche in the Fund (up to SDR 5.5 million) which would become available once arrears were cleared. Once arrears to the Fund are cleared, Cambodia would be in a position to request the use of Fund resources in support of appropriate policies.

Cambodia's medium- and long-term official debt comprises mainly overdue obligations resulting from debt contracted bilaterally before the mid-1970s and obligations to the former Soviet Union contracted since 1979. In respect of both categories of debt, comprehensive data are not available, but efforts are under way to quantify current and future obligations. It is expected that requests will be made for cancellation of the existing debts on a bilateral basis.

During the remainder of 1992 and in 1993 Cambodia will not impose or intensify restrictions on payments and transfers on current international transactions, introduce new multiple currency practices or modify the existing multiple currency practice, conclude bilateral payments agreements

that are inconsistent with Article VIII of the Fund's Articles of Agreement, or impose or intensify import restrictions for balance of payments reasons.

/s/

Chhay Than
Minister
Ministry of Finance

/s/

Cha Rieng
Governor
National Bank of Cambodia

/s/

J. R. Dodsworth
Head of Mission
Central Asia Department
International Monetary Fund

Table 1. Cambodia: Key Economic Indicators, 1988-93

	1988	1989	1990	1991	1992 Program	1993 Program
<u>(Percentage change)</u>						
Real GDP growth	9.8	3.5	1.2	7.6	6.5	8.0
Agriculture	5.9	7.1	1.2	6.7	2.6	6.2
Industry	15.0	1.8	-2.1	8.9	16.2	15.0
Services	13.6	-1.1	2.7	8.4	8.2	7.3
Consumer prices (end of period)	...	109.2	161.8	53.0	213.2	29.6
Consumer prices (period average)	...	70.2	157.3	121.1	81.7	85.9
Domestic liquidity	84.9	81.8	150.7	47.3	167.5	29.1
Bank financing of budget	-9.2	106.8	154.5	65.4	145.7	4.8
Velocity (GDP/liquidity)	16.7	11.3	12.4	15.5	14.4	16.3
Exports (value in terms of US\$) <u>1/</u> <u>2/</u>	22.3	35.7	-21.3	116.9	17.5	12.1
Imports (value in terms of US\$) <u>1/</u> <u>3/</u>	10.2	-10.8	-20.2	-6.1	27.8	88.5
Terms of trade	1.7	43.8	-12.6	1.5	0.2	2.8
<u>(In percent of GDP)</u>						
Budget revenue	4.5	6.4	3.9	4.4	5.1	5.4
Budget expenditure	6.8	9.1	8.4	8.8	10.3	11.8
Current	5.4	7.7	7.2	8.5	9.6	8.7
Civilian	3.5	4.7	4.1	5.0	5.1	5.3
Military	1.9	3.0	3.1	3.5	4.6	3.4
Capital	1.4	1.4	1.2	0.4	0.7	3.1
Current deficit (-)	-0.9	-1.3	-3.3	-4.1	-4.6	-3.2
Overall balance	-2.4	-2.7	-4.5	-4.4	-5.2	-6.4
Foreign financing	1.6	0.8	1.2	0.5	0.5	6.2
Domestic financing	0.7	1.9	3.3	3.9	4.8	0.2
External current account <u>1/</u>						
Including official transfers <u>1/</u>	-6.4	-6.2	-3.5	-1.3	-0.8	-4.4
Excluding official transfers <u>1/</u>	-7.5	-7.4	-6.4	-1.5	-1.4	-7.3
Gross official reserves <u>4/</u>						
In millions of U.S. dollars	0.7	0.4	0.3	0.3	1.0	13.3
In months of imports <u>3/</u>	0.1	--	--	--	0.1	0.6
Exchange rate (riels per US\$, end of period)	142	218	600	520	2,000 <u>5/</u>	...

Sources: Data provided by the Cambodian officials; and staff estimates and projections.

1/ Prior to 1991, the exchange rate of rub 1.1=US\$1 is used for the conversion of nonconvertible currency values. The change to convertible currency in 1991 makes it difficult to meaningfully compare balance of payments aggregates between 1990 and 1991.

2/ Excludes re-exports.

3/ Excludes imports for re-export.

4/ Gross official reserves are the reserves of the National Bank of Cambodia.

5/ As at mid-October.

Table 2. Cambodia: Quantitative Benchmarks Under
the Proposed Stabilization Policies, 1992-93

	Stock at the end of Sept. 1992 (Estimate)	1992 Dec.	<u>1993</u>			
			March	June	Sept.	Dec.
<u>(Maximum cumulative change from end-September 1992)</u>						
Net domestic assets of the banking system <u>1/ 2/</u> (in billions of riels)	220.8	43.0	80.6	87.6	80.9	81.6
Net bank credit to finance budget (in billions of riels) <u>2/</u>	172.4	35.0	62.0	61.4	48.1	44.9
Contracting of nonconcessional public sector or public sector-guaranteed external debt <u>3/</u> (in millions of U.S. dollars) ...		--	--	--	--	--
<u>(Minimum cumulative change from end-September 92)</u>						
Gross official foreign reserves <u>2/, 4/</u> (in millions of U.S. dollars)	--	1.0	10.2	10.6	11.7	13.3

1/ Net domestic assets are defined as total domestic liquidity minus net foreign assets of the banking system, excluding valuation adjustments associated with exchange rate changes. Changes in net domestic assets arising out of the reopening and revaluation of the IMF amounts with the National Bank of Cambodia and the full or partial clearance of arrears to the Fund are excluded.

2/ Benchmarks on net domestic assets and net bank credit to finance budget will be adjusted upward while the benchmark on gross official foreign reserves will be adjusted downward for any cumulative shortfall in external support from its program estimates of US\$ zero million for October-December 1992, US\$4.50 million for October 1992-March 1993, US\$25.15 million for October 1992-June 1993, US\$46.58 million for October 1992-September 1993, and US\$68.85 million for October 1992-December 1993, up to a maximum adjustment of US\$20.00 million. Should there be any cumulative excess in external support from its program estimates, benchmarks on net domestic assets and net bank credit to finance budget will be adjusted downward while the benchmark on gross official foreign reserves will be adjusted upward by the full amount of such an excess.

3/ External debt is defined as nonconcessional debt contracted or guaranteed by the public sector with maturities of 15 years or less, excluding short-term trade credits.

4/ Gross external assets of the National Bank of Cambodia, including IMF reserve tranche if any.

Table 3. Cambodia: External Financing Requirements, 1993-1996

(millions of U.S. dollars)

	1993 Proj.	1994 Proj.	1995 Proj.	1996 Proj.
Uses of Foreign Exchange	-518.2	-395.7	-408.0	-444.4
Imports	-404.3	-350.7	-361.0	-395.0
Service payments	-34.0	-29.0	-31.0	-33.4
Debt-service obligations <u>1/</u>	-4.2	-6.0	-6.0	-6.0
Clearance of Fund arrears	-61.9	0.0	0.0	0.0
Change in net foreign assets	-13.8	-10.0	-10.0	-10.0
Sources of Foreign Exchange	322.8	254.1	267.5	309.2
Exports of goods	240.3	166.1	164.5	181.8
Services receipts	45.5	35.0	37.1	39.4
Private transfers	10.0	15.0	18.0	25.0
Private capital flows	27.0	38.0	48.0	63.0
Financing Requirements	-195.4	-141.6	-140.5	-135.2
Available external financing	195.4	...	...	...
Commodity aid	76.4	...	...	...
Cash assistance <u>2/</u>	61.9	...	...	...
Project aid	57.1	...	...	...
Memorandum items:				
Use of Fund Resources				
Possible Stand-By (in SDR millions)	6.25			
Exports (recorded), percent change	12.1	13.4	16.5	12.7
Imports (retained), percent change	88.5	12.8	9.9	10.0
Current account balance/GDP	-7.3	-7.6	-7.3	-7.0

1/ Debt-service obligations exclude overdues on debt contracted with OECD creditors prior to the mid-1970s and post-1979 debt with the former Soviet Union and Eastern European countries. Efforts are under way to quantify obligations arising from these debts, prior to negotiations with creditors to obtain debt relief.

2/ There are SDR 7.8 million in assets held by the IMF on Cambodia's behalf (including SDR 5.1 million in restituted gold) which can be utilized in partial payments of arrears to the IMF.

Cambodia - Overdue Financial Obligations to the Fund

(As of November 20, 1992)

Type of Obligation	Date of Purchase or Loan	Due Date	SDR Amount
<u>General Department</u>			
1. Principal			
CF-repurchase	3/14/72	03/13/75	6,250,000
GT-repurchase	9/15/71	05/20/75	1,000,000
GT-repurchase	9/15/71	08/20/75	1,000,000
GT-repurchase	9/15/71	11/20/75	1,000,000
GT-repurchase	9/15/71	02/20/76	1,000,000
CF-repurchase	4/18/73	04/17/76	6,250,000
GT-repurchase	9/15/71	05/20/76	1,000,000
GT-repurchase	9/15/71	08/20/76	<u>1,243,538</u>
Sub-total			18,743,538
2. Charges and assessments			
Quarterly charges		05/30/75	96,594
Quarterly charges		08/30/75	110,207
Quarterly charges		11/30/75	115,498
Quarterly charges		03/01/76	125,832
Quarterly charges		05/30/76	128,078
Quarterly charges		08/30/76	141,305
Quarterly charges		11/30/76	146,582
Quarterly charges		03/02/77	157,150
Quarterly charges		05/30/77	157,520
Quarterly charges		08/30/77	173,180
Quarterly charges		11/30/77	174,330
Quarterly charges		03/02/78	181,056
Quarterly charges		05/30/78	175,179
Quarterly charges		08/30/78	189,011
Quarterly charges		11/30/78	189,011
Quarterly charges		03/02/79	189,011
Quarterly charges		05/30/79	182,852
Quarterly charges		08/30/79	189,024
Quarterly charges		11/30/79	189,024
Quarterly charges		03/01/80	188,851
Quarterly charges		05/30/80	184,412
Quarterly charges		08/30/80	188,519
Quarterly charges		11/30/80	188,519

Type of Obligation	Date of Purchase or Loan	Due Date	SDR Amount
Quarterly charges		03/01/81	188,692
Quarterly charges		05/30/81	182,871
Quarterly charges		08/30/81	189,044
Quarterly charges		11/30/81	189,044
Quarterly charges		03/01/82	189,044
Quarterly charges		05/04/82	182,882
Quarterly charges		08/04/82	189,053
Quarterly charges		11/04/82	189,053
Quarterly charges		02/03/83	189,054
Quarterly charges		05/05/83	182,889
Quarterly charges		08/04/83	189,054
Quarterly charges		11/04/83	189,054
Quarterly charges		02/06/84	188,880
Quarterly charges		05/04/84	184,440
Quarterly charges		08/06/84	188,547
Quarterly charges		11/06/84	188,547
Quarterly charges		02/06/85	188,722
Assessment		04/30/85	2,589
Quarterly charges		05/06/85	182,899
Quarterly charges		08/06/85	189,065
Quarterly charges		11/06/85	189,065
Quarterly charges		02/06/86	189,065
Assessment		04/30/86	2,661
Quarterly charges		05/09/86	182,899
Quarterly charges		08/07/86	189,039
Quarterly charges		11/06/86	189,039
Quarterly charges		02/13/87	189,039
Assessment		04/30/87	2,949
Quarterly charges		05/11/87	182,876
Quarterly charges		08/17/87	189,037
Quarterly charges		11/11/87	189,037
Quarterly charges		02/12/88	188,863
Assessment		04/30/88	2,661
Quarterly charges		05/16/88	184,424
Quarterly charges		08/18/88	188,514
Quarterly charges		11/14/88	188,514
Quarterly charges		02/15/89	188,730
Assessment		04/30/89	2,661
Quarterly charges		05/10/89	182,907
Quarterly charges		08/10/89	189,076
Quarterly charges		11/09/89	189,083
Quarterly charges		02/12/90	189,101

Type of Obligation	Date of Purchase or Loan	Due Date	SDR Amount
Assessment		04/30/90	3,093
Quarterly charges		05/14/90	182,943
Quarterly charges		08/16/90	189,098
Quarterly charges		11/12/90	189,100
Quarterly charges		02/14/91	189,075
Assessment		04/30/91	2,661
Quarterly charges		05/10/91	182,898
Quarterly charges		08/14/91	189,072
Quarterly charges		11/13/91	189,063
Quarterly charges		02/14/92	188,882
Assessment		04/30/92	2,949
Quarterly charges		05/12/92	184,434
Quarterly charges		08/13/92	188,533
Quarterly charges		11/12/92	188,526
Sub-total			12,783,659

SDR Department

Net SDR charges	11/01/84	18,353
Net SDR charges	02/01/85	315,359
Net SDR charges	05/01/85	324,590
Net SDR charges	08/01/85	311,152
Net SDR charges	11/01/85	305,843
Net SDR charges	02/01/86	320,282
Net SDR charges	05/01/86	286,459
Net SDR charges	08/01/86	269,709
Net SDR charges	11/01/86	261,428
Net SDR charges	02/01/87	273,017
Net SDR charges	05/01/87	258,930
Net SDR charges	08/01/87	261,190
Net SDR charges	11/01/87	285,814
Net SDR charges	02/01/88	271,521
Net SDR charges	05/01/88	260,464
Net SDR charges	08/01/88	288,865
Net SDR charges	11/01/88	340,299
Net SDR charges	02/01/89	372,987
Net SDR charges	05/01/89	401,797
Net SDR charges	08/01/89	429,442
Net SDR charges	11/01/89	447,977
Net SDR charges	02/01/90	490,220

Type of Obligation	Date of Purchase or Loan	Due Date	SDR Amount
<hr/>			
Net SDR charges		05/01/90	496,286
Net SDR charges		08/01/90	518,984
Net SDR charges		11/01/90	533,734
Net SDR charges		02/01/91	531,110
Net SDR charges		05/01/91	477,843
Net SDR charges		08/01/91	478,304
Net SDR charges		11/01/91	467,071
Net SDR charges		02/01/92	444,706
Net SDR charges		05/01/92	424,740
Net SDR charges		08/01/92	428,687
Net SDR charges		11/01/92	<u>412,549</u>
Sub-total			12,009,712
Total			<u>43,536,909</u>

Cambodia - Overdue and Forthcoming Financial Obligations
as of November 20, 1992

(In millions of SDRs)

Type of Obligation	Overdue as of 11/20/92	Forthcoming 1/					Total Through 1996 3/
		1992 2/	1993	1994	1995	1996	
Repurchases	18.7	--	--	--	--	--	18.7
Quarterly charges 4/	12.8	--	--	--	--	--	12.8
Net SDR charges 4/	<u>12.0</u>	<u>--</u>	<u>1.7</u>	<u>1.7</u>	<u>1.7</u>	<u>1.7</u>	<u>18.8</u>
Total 3/ 5/	43.5	--	1.7	1.7	1.7	1.7	50.4

1/ Estimated on the basis of present use of Fund credit, and Cambodia's present position in the SDR Department. Charges are projected on the basis of current rates of charge applicable to Cambodia.

2/ Due after November 20, 1992.

3/ Totals may not add due to rounding.

4/ Forthcoming charges estimated on the assumption that overdue obligations will be settled at the end of 1992, and forthcoming obligations are settled promptly thereafter.

5/ Includes overdue assessments of SDR 22,224.

Cambodia: Fund Missions to Phnom Penh
(November 1991-October 1992)

Date	Departments and Number of Persons	Purpose
<u>1991</u>		
1. November 24- December 4	CTA (3)	Staff visit with AsDB for familiarization
2. December 8-28	CBD (1) FAD (1)	UN survey mission on administrative structure
<u>1992</u>		
3. January 27- February 8	CTA (2) TRE (1)	Staff visit with AsDB on prospects for normalization and technical assistance
4. March 16- April 4	STA (1) FAD (1)	UN economic assessment mission
5. May 27- June 13	CTA (3) ETR (1) TRE (1)	Staff visit on macro-economic framework and normalization discussions
6. May 30 June 20	FAD (5)	Fiscal mission
7. June 5-17	MAE (4) CTA (1)	Money and banking mission
8. June 8-12	STA (1)	Money and banking statistics mission
9. August 26- September 9	STA (5)	Multitopic statistical mission
10. October 14-28	CTA (4) PDR (1) TRE (1)	Staff visit on stabilization policies

Table 1. Cambodia : Payment Indicators, 1989-92

	1989	1990	1991	1992 (First 6 months)
1. Payments to the Fund	(In millions of SDRs)			
a. Obligations falling due to the Fund	2.4	2.8	2.7	1.3
b. Payments made to the Fund	--	--	--	--
c. Burden sharing refunds	--	--	--	--
d. Arrears to the Fund	35.6	38.4	41.1	42.3
2. Sources of foreign exchange 1/	169.2	177.7	217.6	128.1
a. Current account receipts 2/ (of which: Exports, f.o.b.)	64.9 61.8	66.9 63.2	197.4 184.6	114.5 97.2
b. Official capital inflows (of which: Official grants)	104.3 13.5	110.8 30.7	5.6 1.8	4.1 4.1
c. Direct investment, net 3/	--	--	14.6	9.5
3. Obligations and uses of foreign exchange	153.8	144.9	217.6	125.6
a. Current account payments 4/ (of which: Imports, c.i.f.)	145.5 137.3	127.7 120.5	215.6 208.4	122.4 117.4
b. Debt service payments made 5/ (i) Amortization	8.3 5.8	17.2 10.7	2.0 --	3.2 0.8
(ii) Interest	2.5	6.5	2.0	2.4
4. Gross official reserves 6/	0.3	0.2	0.2	0.1
5. Obligations falling due to the Fund as percent of:	(In percent)			
a. Sources of foreign exchange 1/	1.4	1.6	1.2	1.0
b. Current account receipts 2/	3.7	4.2	1.4	1.1
c. Exports	3.9	4.4	1.5	1.3
d. Obligations and uses of foreign exchange	1.6	1.9	1.2	1.0
e. Imports	1.7	2.3	1.3	1.1
f. Debt service payments made 5/	28.9	16.2	135.5	39.1

Table 1 (concluded). Cambodia : Payment Indicators, 1989-92

	1989	1990	1991	1992 (First 6 months)
6. Arrears to the Fund as percent of:				
a. Sources of foreign exchange <u>1/</u>	21.0	21.6	18.9	33.0
b. Current account receipts <u>2/</u>	54.8	57.4	20.8	37.0
c. Exports	57.6	60.7	22.2	43.5
d. Obligations and uses of foreign exchange	23.1	26.5	18.9	33.7
e. Imports	25.9	31.8	19.7	36.0
f. Debt service payments made <u>5/</u>	428.6	223.1	2,053.5	1,322.4

Source: The Cambodian authorities; and staff estimates.

- 1/ Includes receipts from FSU and COMCON countries values at Ruble 1.1 per US dollar.
2/ Includes exports of goods and services and private transfers; excludes official transfers.
3/ Excludes errors and omissions.
4/ Excludes interest payments.
5/ Debt service obligations exclude overdues on debt contracted with OECD creditors prior to the mid-1970s and post-1979 debt with FSU and Eastern European countries. Efforts are underway to quantify these obligations.
6/ Reserves of the National Bank of Cambodia excluding liabilities to and assets with the IMF.

