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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 88/175

3:00 p.m., December 8, 1988

R. D. Erb, Acting Chairman

Executive Directors

J. E. Ismael
B. Jalan

G. A. Posthumus

K. Yamazaki

Alternate Executive Directors

C. Enoch
C. J. Jarvis, Temporary
Yang J., Temporary
A. Rieffel, Temporary
H. S. Binay, Temporary
L. B. Monyake
R. J. Lombardo
M. A. Fernández Ordóñez
R. Marino, Temporary
F. El Fiky, Temporary
M. A. Hammoudi, Temporary
B. Goos
E. Kiriwat
L. E. N. Fernando
L. M. Piantini, Temporary
D. McCormack
K. Yao, Temporary
I. A. Al-Assaf
B. R. Fuleihan, Temporary
M. Fogelholm
D. Marcel
G. Serre, Temporary
G. P. J. Hogeweg
C. Y. Legg, Temporary
S. Appetiti, Temporary

C. Brachet, Acting Secretary
L. Collier, Assistant

1. Equatorial Guinea - Structural Adjustment Arrangement Page 3
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Following Declaration of Ineligibility Page 15

Also Present

IBRD: P. Alba, Africa Regional Office; K. Ikram, Asia Regional Office.
African Department: G. E. Gondwe, Deputy Director; S. Almuina,
C. P. Andrade, T. T. Gibson, J. R. Hill, J. M. Jiménez, E. K. Martey.
Asian Department: P. R. Narvekar, Director; H. Neiss, Deputy Director;
M. J. Fetherston, G. Szapary, T. Krueger, H. Tokumaru. Exchange and Trade
Relations Department: H. B. Junz, Deputy Director; G. R. Kincaid. Legal
Department: P. L. Francotte, J. W. Head, A. O. Liuksila. Treasurer's
Department: F. G. Laske, Treasurer; T. Leddy, Deputy Treasurer;
J. E. Blalock, P. S. Ross. Special Advisor to the Managing Director:
A. K. Sengupta. Advisors to Executive Directors: N. Adachi,
M. B. Chatah, M. Eran, S. M. Hassan, P. D. Péroz, G. Pineau. Assistants
to Executive Directors: T. T. Do, J. Gold, A. Iljas, K.-H. Kleine,
T. Morita.

1. EQUATORIAL GUINEA - STRUCTURAL ADJUSTMENT ARRANGEMENT

The Executive Directors considered a staff paper on Equatorial Guinea's request for a three-year structural adjustment arrangement in an amount equivalent to SDR 11.7 million and the first annual arrangement thereunder (EBS/88/220, 10/26/88), together with a policy framework paper for Equatorial Guinea (EBD/88/301, 10/26/88). They also had before them a statement by the Managing Director, which read as follows:

There follows for the information of Executive Directors the text of a memorandum that I have received from the President of the World Bank to serve as the basis for my statement on the matter to the Board. This text summarizes the main points covered by the Executive Directors of the Bank and IDA in their November 17, 1988 discussion in Committee of the Whole of a paper entitled "Equatorial Guinea: Policy Framework Paper."

1. The Executive Directors of the Bank and IDA discussed, in a meeting of the Committee of the Whole, the paper entitled "Equatorial Guinea: Policy Framework Paper."

2. Directors expressed general support for the paper, noting that this represented evidence of the Government's determination to consolidate recent important efforts to improve economic performance and macroeconomic balances, to rely more on a market-oriented approach for resource allocation, and to encourage private sector development. Particularly noteworthy were the recently improved fiscal performance and the actions taken to redress the banking sector crises, especially after earlier slippages in reform measures in the last decade. In this connection, continued attention to public finance issues, especially the clearing of domestic arrears, was deemed to be essential.

3. Directors also expressed concern on whether export projections were realistic in light of past difficulties, depressed world markets, and infrastructural deficiencies. It is expected that internal structural improvements will only partially compensate for the depressed state of international markets. The effective implementation of diversification efforts must therefore receive priority. Attention should be given that this is achieved through broad-based local participation and not just foreign-owned enclaves.

4. The Directors welcomed the recent progress in redressing the banking sector problems, including efforts to open an additional bank. They underlined the need to follow appropriate credit policies, and for the new banks to be managed according to traditional banking practices.

5. The weakness of the existing human resource base was noted and the need for technical assistance recognized. Training and human resource development must be given priority. Attention should also be directed toward the adoption of effective policies of environmental protection.

6. Regarding the social impact of adjustment, the Directors felt that while it was difficult to avoid completely the problems arising from adjustment, over time the benefits would greatly outweigh the costs of the reforms. They urged that the social implication of the adjustment program be more carefully defined and monitored.

7. The Directors expressed the view that although the external financing required appeared large in per capita terms, there should be strong support from the international community for Equatorial Guinea during this first phase of its structural adjustment program in view of the need to improve infrastructure and to increase the provision of basic educational and health services to a needy population. In this context, they noted the heavy debt burden and indicated that Equatorial Guinea should be among the countries for which special efforts need to be made to obtain additional support for adjustment in the form of concessional debt relief and further quick-disbursing assistance, possibly in the context of the Special Program of Assistance.

Mr. Yao made the following statement:

My authorities are greatly encouraged by the support of the Fund and are confident that their strategy and ongoing concerted efforts will lead to the restoration of strong economic growth and to a viable external payments position in the medium term.

During the period 1986-88, the economic performance of Equatorial Guinea was hampered by structural rigidities and unfavorable developments in the prices of its major exports. As a result, sluggish economic growth was recorded, and the internal and external imbalances were unsustainably high. Faced with such difficult economic and financial circumstances, the authorities took a number of corrective measures that have had positive effects, particularly on the budgetary outcome. Despite the progress realized on some fronts, my authorities recognize that the attainment of long-term sustainable growth would require the removal of a number of constraints, namely, the reliance on a few export crops; the deterioration in the productive capacity and related infrastructure; and the heavy external debt service burden.

It is against this background that my authorities have decided to adopt a comprehensive macroeconomic program that

contains a wide range of policies aimed at correcting the structural rigidities and reducing the financial imbalances, thereby laying the foundation for long-term sustainable economic growth. The objectives of this program are to achieve an average rate of growth of 3.5 percent during the period 1988-91, contain the rate of inflation, and reduce the overall balance of payments deficit.

My authorities consider that structural policies are an important aspect of the program because key sectors of the economy are beset by structural rigidities. They have therefore placed considerable emphasis on structural measures in the agricultural sector, the provision of incentives to the private sector, and the reform of the public enterprise sector.

In the agricultural sector, the authorities aim at rehabilitating the cocoa subsector and other export commodity subsectors such as coffee and timber as well as increasing food crop production. Recognizing that the attainment of the overall objectives of the program hinges upon an improvement in this sector, the Government has taken steps to allocate a significant proportion of the investment budget--about 39 percent--to this sector and to the maintenance of infrastructure. A number of internal impediments have also been addressed. For instance, in the cocoa subsector, the authorities have introduced a graduated export tax that is linked to the world market price; with the establishment of foreign-owned banks and an IDA-financed loan, the liquidity problem facing most producers has been corrected; a review of the producer price will be undertaken yearly with the assistance of the World Bank; and steps are being taken to reduce the labor shortage by introducing a labor code to attract foreign workers. As regards the timber subsector, a number of incentives have been provided to increase timber production and tax revenue. To that end, the regulating framework has been clarified with respect to production targets, reference prices, and taxation. In addition, the revenue collection procedure has been improved by channeling all export transactions through the commercial bank. In the context of the diversification policy aimed at reducing the dependence of the economy on cocoa and timber, studies are being undertaken to identify constraints and recommend measures to increase the output of coffee and food crops. Also, to stimulate activity in the fishing and mining sectors, the regulations governing these sectors will be revised.

My authorities recognize that an increased role of the private sector in the economy is critical to the attainment of the program objectives. To this end, efforts are being made to provide assurance that property rights will be respected. Furthermore, the new investment code under preparation will clarify the regulating and incentive framework, thereby

increasing the role of the private sector in the economy. Also noteworthy is the progress being made toward greater flexibility in pricing policy.

During the period 1988-91, the authorities intend to continue their efforts to restructure the public enterprise sector. In that regard, a number of enterprises will be liquidated. However, those to be rehabilitated will either be partly or wholly privatized, and their financial situation will be strengthened by allowing the prices of their goods and services to reflect production costs. Moreover, steps are being taken to evaluate the interenterprise arrears with a view to eliminating them gradually.

In support of the structural policies, the Government will follow prudent fiscal and monetary policies. In the fiscal sector, the authorities are committed to a further reduction in the budget deficit in 1988 and to achieve a surplus by 1991. Even though this objective seems ambitious, the Government believes that it can be achieved through the strengthening of the tax system and its administration, and the monitoring and control of expenditure. To address the lack of qualified personnel--an essential element in the achievement of the fiscal objective--my authorities have given high priority to training and human development.

As described in the policy framework paper, the fiscal measures that are to be implemented include the abolition of ad hoc exemptions from customs duties; upward revision of the domestic turnover tax; the establishment of quarterly limits on the wages and salary bill; and the reduction of subsidies to the public enterprise sector.

Regarding monetary and credit policies, my authorities are aware of the challenge that the liquidation of the two bankrupt banks poses to the confidence in the banking system. In that context, while appropriate steps are being taken to reimburse private depositors, improve the recovery of assets, and finalize the agreement with the Banque des Etats de l'Afrique Centrale (BEAC) on the outstanding debt, the monetary and credit targets under the program will provide adequate liquidity to the economy with due regard to private sector financing needs.

Consistent with the orientation of the medium-term framework, the authorities have set the following objectives for the 1988-89 adjustment program: to achieve real economic growth of 3.5 percent; to contain the rate of inflation to about 4 percent; and to reduce the external current account deficit to a sustainable level.

The set of policies that will enable the authorities to achieve these objectives are well described in the staff paper. These measures place emphasis on the restructuring of the economy toward production of exportable goods, in an environment where prudent demand-management policies will be implemented.

To conclude, I would like to stress my authorities' concern about the deteriorating economic and financial situation of Equatorial Guinea and reiterate their commitment to redress this situation by implementing a comprehensive macroeconomic program. While the comprehensiveness of the set of measures envisaged will be instrumental in setting the stage for long-term sustainable growth, the support of the international community will be critical to the successful implementation of the program. Therefore, I urge the international community to provide the necessary technical and financial support.

Mr. Jarvis made the following statement:

I commend the authorities for the steps they have taken to deal with imbalances in the economy and to address structural problems. The authorities' commitment to a sound fiscal policy is particularly important. While the underlying trend has improved this year, it is important that restraint should continue to be exercised in current expenditure--especially wages and salaries--and that the measures for broadening and increasing the revenue base outlined in the paper should be adopted. In particular, the move away from taxes on production and toward taxes on consumption is welcome.

The plans for monetary policy seem to be sound. Clearly, the banking system is still recovering from the bankruptcy of the two major banks. The move to introduce a foreign-owned bank is a useful step in restoring confidence in the system.

My main concern rests with the external sector policies and balance of payments outlook described in the staff paper. The current account balance shown in Table 4 of the paper has been strongly negative in every year except the present one--when large net transfers produced a surplus--and is expected to continue to be strongly negative. Exports have almost doubled since 1985, but about half of the increase is due to better recording of re-exports rather than to a real improvement in the balance of trade.

Moreover, there is a significant financing gap over the period of the program. The staff reports that this should be filled by more money from donors and debt rescheduling, but I understand that not all of the debt falling due over the program period is susceptible to rescheduling; I would be interested in

hearing further details. The sensitivity analysis included in the paper showed how the financing gap would be reduced if prices of cocoa rose or if petroleum prices fell; but there could also be adverse movements in the prices of these commodities. I would welcome reassurance that the program would not be jeopardized in this event.

Despite these reservations, the program is generally a good one. It presents a thorough and credible plan for dealing with Equatorial Guinea's structural problems. I would particularly like to stress the importance of incentives, especially for agricultural producers, which is recognized in the program. In many countries, serious problems have developed from high taxes on producers--either direct taxes or through artificially low producer prices. I strongly commend the authorities' decision last year to link the level of export taxes to world prices so as to protect producer prices. Incentives for producers are necessary to increase output, thereby helping to solve revenue and balance of payments problems in the long term. This is true for both the food crops that the program aims to promote and for cash crops. I can support the proposed decision.

Mr. Fernández Ordóñez said that he supported Equatorial Guinea's request for a structural adjustment arrangement. In doing so, he had taken three factors into account: first, the difficult situation of the Equatorial Guinean economy, the causes of which were described in the staff report; second, the positive attitude of the Equatorial Guinean Government, as shown by the recent adoption of necessary adjustment measures, especially those to balance the budget, restore confidence in the financial system, and improve public sector planning; and third, the well-designed three-year program put forward by the Government to be supported by the World Bank and the Fund. The commitment of the Government with regard to fiscal policy, the emphasis on private sector incentives, and the institutional arrangements aimed at increasing foreign investment were particularly noteworthy.

Nevertheless, it was also necessary to take into account the member's disappointing performance under previous Fund arrangements, Mr. Fernández Ordóñez remarked. In fact, Equatorial Guinea's experience was similar to that of other small countries where problems had resulted not from a lack of external resources--which could have been provided by donors--but from the lack of administrative capacity and of persistence in fulfilling commitments. He therefore welcomed the planned technical assistance and the authorities' intention to implement the program fully; those factors were vital for the program's success. The multilateral institutions could play a central role, and in that connection a strengthened monitoring of the program would be important.

Mr. Goos observed that it was clear from the staff paper that unless the many structural impediments were adequately and consistently addressed, Equatorial Guinea's medium-term growth prospects would remain unfavorable and its debt service burden would remain high. The weakness of the human resource base was perhaps the most serious obstacle; in that context, much needed to be done to improve administrative capacity--a key requirement for successful program implementation. He therefore hoped that the reform measures already initiated in the civil service would produce a decisive turnaround in the situation. Substantial technical assistance would be required to improve not only the skills and motivation of the civil service, but also the inadequate statistical data base. He therefore welcomed the indications that technical assistance would be provided by the Fund and the World Bank. Without a more reliable data base, which was of critical importance for the successful design, implementation, and monitoring of economic policy, it would be premature to consider a possible arrangement under the enhanced structural adjustment facility. He wondered why the issue of the data base, together with the shortcomings of the administrative capacity of the country, had not been addressed more forcefully under the previous stand-by arrangements with the Fund.

The program under consideration seemed to point in the right direction, Mr. Goos remarked. If fully implemented, it was likely to make a tangible contribution to improving the country's difficult economic prospects. It would also pave the way for an appropriate flow of concessional external assistance. Like Mr. Jarvis, he was interested in the staff's comments on how the worrisome financing gaps would be closed. He hoped that in the period ahead the authorities would demonstrate their ability to implement with determination and persistence the policies outlined in the policy framework paper. In that regard, the upcoming Article IV consultation discussions would provide an early opportunity to monitor program implementation. He endorsed the staff appraisal and supported the proposed decision.

Mr. Rieffel said that he shared the staff's appraisal and supported the proposed decision. The initial phase of the three-year program contained quite a few studies, which he hoped would not be delayed. He would look carefully at how the results of those studies would be implemented when the Board reviewed Equatorial Guinea's request for a second annual structural adjustment arrangement. In the same vein, he noted that an Article IV consultation could have been scheduled to coincide with the present request, although doing so would have left a long gap between staff visits. Accordingly, he supported deferring somewhat the Article IV consultation to provide a good opportunity to review progress under the first annual arrangement and to ensure that the program remained on track.

Finally, he had a familiar procedural concern, Mr. Rieffel said. He had not found in the staff paper an explicit assessment of Equatorial Guinea's capacity to repay the resources it was requesting. From the information provided, he did not see a problem. He also recognized that much of the work on the paper had been done before the Executive Board had

completed its report to the Interim Committee on overdue obligations, which gave some prominence to such assessments. Nevertheless, he would welcome any additional comments by the staff on that subject.

Mr. Serre made the following statement:

This chair welcomes Equatorial Guinea's request for a structural adjustment arrangement as a decisive step toward its economic recovery. Indeed, since 1983 the authorities have been carrying out a major program of economic reform and adjustment, including membership in the BEAC. However, Equatorial Guinea's growth has been hampered by structural bottlenecks such as the lack of trained administrative personnel, inadequate economic planning and budgeting policies, the concentration of production and exports on a few crops, and an illiquid financial system.

To overcome these bottlenecks, the authorities have adopted an adjustment program as part of the medium-term policy framework, which was designed to establish a sound basis for economic growth and to strengthen the balance of payments. The perspective of this medium-term framework provides the only way to address structural imbalances, and we commend the authorities for taking this approach.

With regard to macroeconomic policies, much effort is needed in the budgetary area. A reduction of the financial imbalances is of the utmost importance, and we urge the authorities to implement as soon as possible the new fiscal measures aimed at limiting the overall fiscal deficit. We are also concerned about the emergence of arrears between the Government and public enterprises, between the Government and the private sector, and among public enterprises. These arrears must be inventoried promptly to avoid a further misallocation of resources; the elimination of arrears is of paramount importance for the medium-term strategy. In this regard, more information on the Treasury's position vis-à-vis the public enterprises would be appreciated.

As for monetary and credit policies, we welcome the current process of re-establishing confidence in the banking system by restoring its liquidity to a level adequate to meet the working needs of the economy and promoting its remonetization. In addition, we urge the authorities to pay close attention to the structure and level of interest rates so as to maintain the attractiveness of holding liquid assets.

In respect to structural reform, it is necessary to gather more information on the country's basic economic needs and to establish a reliable data base through the various studies proposed in the policy framework paper. We hope that these studies will provide guidance on increasing traditional export

crops as well as new items like timber, mining, or fishing products. In this regard, close monitoring of the rolling three-year investment program will help to attain the targeted rate of growth without further slippages. Stringent implementation of structural measures and macroeconomic policies will allow the international financial community to support Equatorial Guinea's adjustment program through debt rescheduling and additional financing. We support the proposed decision.

Mr. Fuleihan made the following statement:

Since the present Government took office in 1979, it has had mixed success in managing an almost bankrupt economy that had suffered a drain on human resources and experienced substantial internal and external imbalances. The authorities' recent efforts to improve economic performance and to impart greater market orientation to the economy are to be encouraged. Within the framework of the proposed structural adjustment arrangement, the authorities are undertaking the daunting task of intertwining an adjustment program with a far-reaching development strategy.

Immediate attention should be accorded to consolidating recent progress in the fiscal sphere. The authorities correctly recognize the need to reduce the dependence of government revenues on trade duties. I therefore welcome the attempts to improve the regulatory framework and tax procedures in the timber industry. More important, I endorse the attempts to reorganize the Tax Department with a view to strengthening tax collection and administration. This notwithstanding, the main burden of fiscal consolidation will need to fall on expenditure restraint. Enhanced expenditure monitoring and controls are imperative in this regard.

Another area that requires immediate attention is the financial sector. The restoration of confidence in the banking system is crucial to enhance the role of the private sector. The authorities' efforts to liquidate the bankrupt banks and establish a new commercial bank with foreign participation should help. Nonetheless, the authorities will need to orchestrate a delicate monetary policy that restores an appropriate liquidity level without jeopardizing public confidence.

It is evident that the economy is operating well below its potential. However, it is equally evident that the process of improving economic performance will be long and tedious and that the present medium-term program is only a first step, albeit an important one. The main objective in this regard should be the diversification of the economic base. Hence, I support the proposed studies of the coffee, food crops, fishing, and mining

subsectors, with a view to developing nontraditional exports and reducing the heavy dependence on food imports.

Enhancing the role of the private sector will greatly facilitate this objective. Therefore, I endorse the intention to reassess the land tenure system and to facilitate foreign and domestic investment. However, some care will need to be exercised in order to ensure broad-based local participation in this respect. While a greater role for the private sector is crucial, the public sector should maintain its efforts to revamp the economy's infrastructure. Thus, it is essential to improve public investment programming.

The initial phase of the program contains a series of studies, and it is imperative that the authorities rapidly and effectively implement the recommendations of these studies, especially given the authorities' track record regarding the sustained implementation of adjustment policies. Finally, I support the proposed decision.

Mr. Binay observed that although Equatorial Guinea was richly endowed with natural resources it remained only at the threshold of development. The reasons were mainly historical. The country's small population and low levels of household income had until recently operated against the development of a prosperous market economy. Since Equatorial Guinea's small domestic economy did not permit, through economies of scale, the establishment of industries to ensure the efficient allocation of resources, the country's best avenue toward development seemed to lie in concentrating on foreign trade free of restrictions. That solution would require administrative skill in the management of customs and an import tariff regime responsive to fluctuations in the exchange rate and to the changing needs of the economy. Given those prerequisites, foreign trade was capable of creating both revenue and jobs for Equatorial Guinea.

He would like to have more information about the causes of the recent financial crisis that had nearly paralyzed the economy and that continued to hinder it in the near term, and about the measures the Government intended to take against a recurrence, Mr. Binay said. With respect to fiscal policies, the 1989 program seemed to focus on raising existing tax rates to the exclusion of improving tax administration and collection. He would appreciate some comments from the staff on the supply-side effects and the effects on private enterprise of such an approach, and on the ability of the Administration to introduce a progressive income tax instead of a flat-rate tax, the implementation of which had not been optimal.

The problems faced by Equatorial Guinea were deeply rooted and their solution, therefore, would require time as well as resources, Mr. Binay commented. In the absence of a discovery of petroleum or other precious

commodities, those resources would have to include an extraordinary level of assistance from the international community.

The staff representative from the African Department recalled that during the discussions with the authorities, the staff had had difficulty estimating the type of support that Equatorial Guinea could generate from creditors and donors: as indicated in the paper, in the past few years the country had made many false starts in trying to adjust its economy. In fact, the projections prepared by the staff were conservative; the degree of donor support that had emerged at the donors' conference held some ten days previously had been surprising. In effect, a problem that might be faced during the program period would not be how to fill the financing gaps but how to keep the Government from spending quickly the available resources on projects that would not provide the needed returns. In addition to the assistance being provided by various donors, Equatorial Guinea's request for Paris Club rescheduling, to be discussed in January, would apparently be well received; because of the country's income level and high debt service ratio, it fell under the Toronto initiative. The assistance provided by both debt relief and balance of payments support would appear to more than cover the gaps for the near future.

In the staff's projections, a financing gap appeared at the end of the grace period of the first Paris Club rescheduling, the staff representative continued. However, the staff believed that if the authorities implemented the current program with vigor, by 1991 they would be in a much better position to tackle that financing problem.

The sensitivity analysis prepared by the staff included both plus or minus variations, and the likelihood of a negative downturn of export prices was a factor that had been taken into account, the staff representative remarked. The authorities were reviewing those developments on a regular basis, and they were committed to taking the necessary steps in the case of a worsening situation.

The staff agreed with those speakers who observed that there was a need to strengthen the monitoring procedures under the program, the staff representative said. For that reason, the scheduling of the Article IV consultation had been delayed to allow an interim review of developments under the program and to give the staff a major role in the preparation of the budget for the coming year.

It had been suggested that insufficient attention had been paid to the data base and administrative shortcomings under previous arrangements, the staff representative noted. Unlike the situation in 1980, current monetary and fiscal statistics were available and rudimentary balance of payments statistics were maintained, although gaps still existed in the real sector. Nevertheless, the studies scheduled under the program would be an important element in filling those gaps and in establishing a current system under which data could be collected for those areas.

Similarly, the administrative shortcomings faced at present were much less severe than those that had prevailed previously, the staff representative observed. In the early part of the decade, few members of the public administration had a secondary education, and those with a higher education had been trained mainly in Eastern bloc countries and were not inclined toward a market-oriented economy. A significant number of changes had been implemented, but the amount of additional changes needed was equally large, reflecting the difficulty of the situation when adjustment had begun.

With respect to the country's ability to repay the Fund, the staff believed that the improvement in Equatorial Guinea's medium-term situation and its debt-servicing capacity largely rested on its ability to implement the commitments under the present program and on the external assistance that such implementation would be able to generate, the staff representative remarked. In the program period, Equatorial Guinea was scheduled to repay all the regular resources drawn, and at the end of the arrangement, its outstanding use of Fund resources would be equivalent to only about 68 percent of quota. At the same time, the program anticipated a buildup of international reserves by a substantial margin, which would provide liquidity and in a sense guarantee timely repurchases by Equatorial Guinea.

The financial crisis was largely the result of two commercial banks' participation in loans for projects that had not been studied and in many cases had not proved viable, the staff representative said. The illiquidity that had arisen from that mismanagement in the banking system had quickly led to the banks being unable to honor checks drawn upon them, and consequently to the inability of people to pay their taxes because their deposits were frozen in the banks. Thus government revenues for various periods under discussion had fallen below the projected amounts. The economy had resorted to barter and to the use of currency in circulation as the only means of transactions. That period had been difficult and had been partly responsible for some of the budgetary problems in previous years highlighted in the paper. In view of the country's weak administrative capacity, the authorities would not be able to implement easily all the improvements in the tax system, and the staff foresaw that progress would be slow and would require technical assistance. In that connection, the Fund would be providing an expert to improve tax administration.

The authorities were in the process of establishing an inventory of the arrears between public sector enterprises, and the initial reduction of those arrears was expected early in 1989, the staff representative from the African Department explained. The Treasury would repay some of its outstanding arrears under the 1989 budget, while the enterprises were being compelled to improve their financial position so that they could meet their liabilities not only to other public enterprises but also to the private sector.

Mr. Yao said that he shared the view of Directors that, given the weak economic and financial situation of the country, the authorities had no other option to improve the economic prospects but to implement the structural reform and financial program cautiously but firmly. The authorities also hoped that technical and financial assistance from the international community would be forthcoming so as to facilitate the adjustment process.

The Executive Board then took the following decision:

1. The Government of Equatorial Guinea has requested a three-year structural adjustment arrangement, and the first annual arrangement thereunder, under the structural adjustment facility.
2. The Fund approves the arrangements set forth in EBS/88/220, Supplement 1.

Decision No. 9036-(88/175), adopted
December 7, 1988

2. VIET NAM - OVERDUE FINANCIAL OBLIGATIONS - REVIEW FOLLOWING
DECLARATION OF INELIGIBILITY

The Executive Directors considered a staff paper on the further review of Viet Nam's overdue financial obligations to the Fund following the declaration of its ineligibility to use the Fund's general resources effective January 15, 1985 (EBS/88/246, 11/30/88; and Sup. 1, 12/5/88).

Mr. Ismael made the following statement:

My Vietnamese authorities express their deep regret that up to today's review, they have not been able to settle their overdue financial obligations to the Fund. Viet Nam's official international reserves remain at the low end-1987 level of \$15 million, just enough for two and one-half weeks of imports or sufficient only to cover approximately one seventh of Viet Nam's arrears to the Fund.

Meanwhile, as indicated by Mr. Le Van Chau in his statement in August 1988 (EBM/88/127, 8/25/88), and fully confirmed by the staff paper under consideration, not only have economic reforms been introduced but the pace has been noticeably stepped up in recent months. The most recent reform was the devaluation of the dong on November 10 by 86 percent, thereby making it worth 56.5 percent of the prevailing black market rate for the U.S. dollar.

It must be recognized, however, that those efforts had to be pursued cautiously owing to various obstacles and

difficulties caused by the vagaries of the weather and the orthodoxy of the prevailing political and economic system. Nevertheless, significant economic improvements have been achieved, but they are still far from sufficient to enable Viet Nam to grow out of its debts.

Notwithstanding the difficulties in clearing the arrears to the Fund, my Vietnamese authorities remain committed to seeking full and prompt settlement of their overdue financial obligations to the Fund and to according the resolution of this problem the highest priority. Under the country's circumstances, this can only be achieved if Viet Nam's assets held in blocked accounts in U.S. banks are released. In light of the recent intensified collaborative guidance provided by the Interim Committee to resolve protracted arrears to the Fund, my Vietnamese authorities would like to appeal anew to the U.S. authorities, and for the intermediation of the Fund, for the release of those assets direct to the Fund for the explicit purpose of fully and promptly settling Viet Nam's overdue financial obligations to the Fund.

Moreover, considering the new sociopolitical and military developments in Viet Nam, and as a response to the recently outlined framework for intensified international collaboration, my Vietnamese authorities are now prepared to embark on the adoption and implementation of a medium-term program of comprehensive economic reforms. My authorities herewith request that a full Fund mission be sent to Hanoi in January 1989 to discuss and help design this comprehensive program.

My authorities express the hope that their present proposals, which form the first two key elements of the intensified collaborative approach, will be received with full understanding and meet with the Executive Board's approval. It is their hope as well that the realization of these proposals will lead to the attainment of the third key element, namely, the restoration of normal relations between Viet Nam and the Fund in the context of Executive Board approval of an arrangement involving the use of Fund resources in support of Viet Nam's adjustment program.

In order that the two proposals contained in this statement can be better reflected in the decision, I would, therefore, propose that paragraphs 3 and 4 be amended. In paragraph 3, the first sentence should read: "The Fund welcomes the economic reform measures implemented recently by Viet Nam and its desire to adopt and implement a comprehensive and realistic adjustment program aimed at achieving sustained economic growth and balance of payments viability." In paragraph 4, the rest of the sentence should be deleted, so that it ended with the word "decision."

Mr. Yamazaki made the following statement:

In the discussion for Viet Nam's 1988 Article IV consultation (EBM/88/84, 5/25/88), this chair stressed the need for the authorities to tackle comprehensively the economic distortions that are deep rooted in the economy. In this respect, we welcome the progress made by the authorities since May. We are also encouraged by the positive statement made by Mr. Ismael. Tightened credit policy coupled with reform measures--including both structural and exchange market reforms--have improved the economic situation. The economy expanded, and improvement on the supply side slowed inflation, although the inflation rate remains high.

Nevertheless, Viet Nam's economy is still suffering from largely deteriorating external and domestic imbalances. We regret the lack of comprehensive measures that could provide a sound financial basis for growth-oriented adjustment.

With respect to arrears to the Fund, we are disappointed that Viet Nam has not made any payments since May 1988. We are also concerned that, in 1988, the authorities made only nominal payments to the Fund while they remain current with some of their creditors.

We have heard repeatedly Viet Nam's intention to restore a normal relationship with the Fund. However, past experience has worsened the creditworthiness of the authorities. In this regard, we particularly welcome the authorities' request for a Fund mission to discuss the intensified collaborative approach, including elements of a possible shadow program. We encourage the authorities to take bolder steps toward strict financial discipline and economic incentives. Meanwhile, we urge the authorities to resume their repayments to the Fund as a sign of their commitment to the collaborative approach.

As the staff noted, the Board will consider the modalities of the intensified collaborative approach, including remedial measures, early in 1989. I would regret it if we should have to consider Viet Nam's overdue financial obligations within three months in light of that discussion. I support the decision with paragraph 3 amended by Mr. Ismael, but retaining paragraph 4 as drafted.

Mr. Marcel noted that the staff paper conveyed the impression that some potentially significant developments had taken place over the recent period. It was difficult, however, to make a clear assessment of the economic situation since the most recent performance appeared mixed. Some headway had been made in certain areas--a relative slowdown of

inflation, and better monetary control--while continued deterioration had been registered in the fiscal and balance of payments areas.

The conclusion might be drawn that the authorities were stepping up their efforts to come to grips with the daunting problems of the Vietnamese economy, Mr. Marcel continued. However, they remained unable to formulate and implement, in an integrated manner, a full-fledged adjustment program. As a result, progress could only be partial and precarious, and the implementation of the collaborative approach to Viet Nam's arrears should be explored. He therefore endorsed the staff mission, scheduled for January 1989, with a view to elaborating a comprehensive adjustment program. Depending on the outcome of that mission, it would then be possible to decide on the implementation of a collaborative approach. In that regard, he wondered whether a comprehensive adjustment program would take the form of a policy framework paper.

The authorities' apparent willingness to take the necessary steps to redress the economic situation was not enough to normalize Viet Nam's relations with the Fund, Mr. Marcel stated. More convincing efforts should also be made to reduce the amount of outstanding arrears at a time when Viet Nam was making rather significant payments to other creditors. A resumption of partial payments to the Fund would facilitate the adoption of the collaborative approach in favor of Viet Nam. He could go along with the amendment proposed by Mr. Ismael for the third paragraph of the proposed decision.

Mr. Goos said that he also regretted that Viet Nam had not yet developed the kind of comprehensive adjustment program recommended repeatedly by the Board that seemed to be essential to stabilize the country's domestic and external financial situation. At the same time, he recognized, like previous speakers, that the authorities had recently adopted a number of important and commendable reform measures. However, to be effective those measures needed to be supplemented by more vigorous efforts at restoring financial discipline, which would necessitate in the first instance decisive steps of fiscal adjustment. Moreover, the structural reform measures, including the correction of relative prices, needed to be invigorated in the framework of a comprehensive program.

Against that background, he welcomed the authorities' willingness to develop such a program as part of the intensified collaborative approach and their invitation to the staff for a full-fledged mission in January 1989, Mr. Goos continued. He also noted the remarkable proposal that the blocked accounts should be released directly to the Fund. Those developments were encouraging.

He agreed with Mr. Marcel that, before formally initiating the collaborative approach, and apart from maintaining good and close working relations with the Fund, the authorities should demonstrate their willingness to restore normal relations with the institution by promptly resuming payments to the Fund and by taking additional adjustment measures, notably in the critical area of the budget, Mr. Goos stated. The substantial

widening of the fiscal deficit in the recent past and the total lack of any payment against the arrears to the Fund were difficult to reconcile with the authorities' alleged recognition of the preferred creditor status of the institution. As Viet Nam had been in arrears to the Fund since 1984, the Board should be prepared to consider more far-reaching measures at its next review of the matter unless substantial progress had been made by that time in stabilizing the economy and in clearing those arrears.

Mr. Enoch made the following statement:

The points that were made during the discussions for our previous review of Viet Nam's arrears (EBM/88/127, 8/25/88) and for the 1988 Article IV consultation (EBM/88/84, 5/25/88) remain generally valid. Since then, however, there have been a number of encouraging signs on the economic front, most important perhaps the significant depreciation of the currency on November 10 and the commitment to continue adjustments in line with movements in the parallel market. These developments, together with the establishment of a legal framework for private economic activities, including permission to engage in foreign trade, and the various other reforms introduced over the past months offer some prospect for the revitalization of Viet Nam's export industries.

Nevertheless, the fiscal position has continued to deteriorate, and it is far from clear that the authorities have any commitment yet to the establishment of the comprehensive adjustment program that is so badly needed. Moreover, there is no reference in the staff paper to Alternative II--the authorities' program for settlement of overdue obligations to the Fund--which we had used as a framework in our earlier discussions. Although the annualized inflation rate of 900 percent for the first half of the year has dropped to 150 percent in recent months, this was due largely to seasonal factors, and the underlying rate probably remains much higher. There has been some improvement in monetary and credit policies, but much more remains to be done. I therefore welcome Mr. Ismael's positive statement concerning his Vietnamese authorities' intention to start implementing a comprehensive adjustment program, and their invitation for a full-fledged staff mission to Hanoi in January 1989.

As regards Viet Nam's arrears to the Fund, unfortunately no payments have been made since May 1988. This seems particularly regrettable as the Director for International Relations at the central bank attended our discussion on the last occasion, and he had the opportunity to hear the emphasis we placed on payments to the Fund as an indication of the commitment to cooperate with this institution.

As this chair has argued in previous discussions, Viet Nam's arrears to the Fund, while significant both to the country and to this institution, are of a magnitude that, if appropriate policies were in place and the commitment to maintain these policies were demonstrated, financing could probably be put together relatively easily. As such, Viet Nam's arrears, perhaps more than those of some other members, are largely a self-imposed problem.

The table on page 4 of the staff paper showing the various debt service payments Viet Nam has made this year is useful and offers some interesting insights. However, in our concern to identify debt service payments made, we should also bear in mind that they are not the only discretionary expenditures made by a country's authorities. In the case before us, imports from the convertible currency area have risen by 54 percent this year. The table on page 2 of the staff paper indicates that Viet Nam's entire arrears to the Fund could have been cleared had the rate of increase of imports for 1988 alone been constrained to rise at about half their actual level; that is, at least in a cash flow sense, Viet Nam could have fully cleared its arrears to the Fund and still have permitted a 20 percent rise in imports for the year. While this would not necessarily have been a preferable, or even feasible, outcome--I would be grateful for any further information the staff can provide on the composition of these additional imports--this shows that we have to look beyond debt service obligations to other creditors to assess a country's ability to pay.

As regards the proposed decision, a clear reference should be made to the Board's forthcoming discussion on the modalities of the intensified collaborative approach, perhaps with the addition of a sentence at the beginning of paragraph 4, along the lines of the previous decision on Viet Nam, stating explicitly that "The Fund is discussing its policies on arrears to the Fund." The intensified collaborative approach could be an attractive incentive for Viet Nam, and one that should be made clear to the authorities. But the remedial measures, in case the incentive is not taken, also need to be highlighted. Overall, I can go along with Mr. Ismael's suggested amendment to paragraph 3 but cannot support his amendment to paragraph 4.

Mr. Legg made the following statement:

Viet Nam may not be the most significant case of overdue obligations in terms of size but it is clearly one of the most frustrating, particularly given the duration of the problem and our impression that, despite the many structural distortions and economic and political difficulties confronting the country, the

fundamental wherewithal exists in parts of the economy for a substantially better performance.

At the time of the 1988 Article IV consultation, the emphasis had been on the lack of domestic consensus in favor of the necessary program of reform. Against this background, the policy changes indicated by the staff and Mr. Ismael are particularly welcome. So too are the various indications that the Vietnamese authorities acknowledge the Fund's preferred creditor status and are ready and eager to participate in the collaborative approach to resolving their arrears.

As is well known, this chair continues to have mixed feelings about the question of ability versus willingness to pay. Irrespective of the causes of a member's current difficulties, the central issue is how to proceed to rectify the situation. I am attracted to the view expressed by Mr. Goos at an earlier meeting that the central test in these cases should be a willingness to cooperate.

In previous reviews of Viet Nam's overdue obligations, the authorities repeatedly referred to their interest in pursuing Alternative II as a means of resolving their arrears problem, but apparently it has now been subsumed, in the view of the authorities, within the Fund's new collaborative approach. Nevertheless, a process of rebuilding credibility is required for the Fund to be satisfied that the test of cooperation can in fact be met. The recent policy initiatives go some way toward this, but they remain piecemeal and fall short of the necessary comprehensive reform program. I strongly urge the authorities to pursue this objective more vigorously in discussions with the forthcoming Fund mission, and I welcome Mr. Ismael's indication that this will be the case.

Another element in the process of rebuilding credibility would be some partial repayment to the Fund as a sign of goodwill. It does not sit well with the authorities' declared enthusiasm for the collaborative approach that no repayments have been received since May. I would see it as a positive sign if, as a minimum, Viet Nam were to recommence meeting all future obligations as they fall due. I recognize, of course, that there is some truth to Mr. Ismael's comments regarding Viet Nam's access to its overseas assets.

With regard to the proposed decision, I have no difficulty with the amendment proposed by Mr. Ismael for paragraph 3. Like Mr. Yamazaki and others, however, I would prefer to leave paragraph 4 as drafted. Finally, notwithstanding the encouraging indications emanating from Viet Nam, we are rapidly approaching the point where, in the absence of real progress, remedial action will need to be seriously considered.

Mr. Marino said that his chair welcomed the adjustment efforts made by the Vietnamese authorities in recent months. He was favorably impressed by the improved output performance and recent deceleration of inflation, but he was concerned about the widening external current account deficit and the deterioration of the fiscal position.

His chair attached great importance to the prompt settlement of overdue obligations to the Fund, Mr. Marino stated. He recognized that the scarcity of foreign exchange in the Vietnamese economy forced the authorities to determine its optimum use according to some criteria. In the past, an important factor had been the need to maintain access to essential imports. He hoped that under the proposed collaborative approach to the settlement of arrears to the Fund, the Vietnamese authorities would find that, in an overall context, the best use of foreign exchange was to eliminate their arrears to the Fund. He thus welcomed the authorities' decision to reach a prompt agreement with the Fund on the formulation of a comprehensive adjustment program. He accepted the proposed amendment to paragraph 3, but like other speakers he would prefer to leave paragraph 4 as drafted.

Mr. Jalan said that he was pleased to note the positive developments in Vietnamese policy as well as the assurances given by the authorities, particularly the invitation to have a Fund team visit the country in order to work out a comprehensive program. He therefore supported the draft decision; he had no difficulty with the modifications suggested by Mr. Ismael in both paragraphs 3 and 4.

Mr. Rieffel made the following statement:

The summary of our previous discussion of Viet Nam's overdue obligations notes the "disappointment and frustration" of Directors at Viet Nam's continued failure to settle its arrears. Since then, no payments have been received from Viet Nam, and no credible program has been formulated. Consequently, our feeling of disappointment and frustration is deeper than ever.

Regarding Viet Nam's economic policies and performance, we are encouraged by the exchange rate action taken by the authorities at the beginning of November. Nevertheless, economic performance in 1988 has generally been mixed, and policy reforms are being pursued in a piecemeal fashion. We regret that the authorities did not take advantage of the recent staff visit to begin serious discussions on medium-term objectives for an economic reform program.

As to Viet Nam's ability and willingness to meet its financial obligations to the Fund, we appreciate the information provided in the staff paper on payments made to the convertible currency area in the first nine months of 1988. I have five reactions to this information.

First, we welcome the recognition by the authorities of the status of the Fund as a preferred creditor and believe this recognition should be reflected in the language of the Board's decision, as was done in the case of Panama a week ago (EBM/88/171, 11/23/88). However, Viet Nam's payment record in 1988 does not appear to be consistent with this attitude.

Second, I am impressed by Viet Nam's ability to make debt service payments in convertible currencies. The information provided constitutes clear evidence that Viet Nam has the ability to pay the Fund more than the \$1.0 million paid in the first nine months of this year.

Third, we would like to have more information on the payments made to the nonconvertible area for our next review of Viet Nam's arrears.

Fourth, I was struck by the large payments made to bilateral official creditors and to private banks. We would like more information on these payments also. For example, has Iraq provided debt relief to Viet Nam, or do these payments represent full contractual amounts on market terms?

Fifth--and anticipating the forthcoming discussion of the semiannual report on overdue obligations--we hope that the Board will agree that information using the various criteria that the staff has suggested for assessing the member's ability to pay will be included in the staff paper for the next review.

Apart from these technical points, however, my authorities are most concerned about the absence of any payments by Viet Nam since the last review. In light of the information provided by the staff, I can only conclude that Viet Nam is not cooperating with the Fund in seeking to fulfill its obligations as a member. In fact, without a material adverse change in its balance of payments position, Viet Nam is in a position to at least meet all forthcoming obligations as they fall due. In the remainder of 1988, for example, there is less than SDR 50,000 in Trust Fund interest falling due, and the payments projected for 1989 amount to less than SDR 1 million a month. If Viet Nam is unwilling to resume meeting these obligations on a current basis, I seriously question the utility of sending a mission to Hanoi in January. In addition, the Board should begin giving serious consideration to remedial measures if progress in this regard is not evident by the time of the next review.

We are encouraged by the interest of the Vietnamese authorities in the intensified collaborative approach and by the statement made by Mr. Ismael. We fully agree that a critical step in this approach is the adoption of a shadow program, and we hope that the mission in January will be able to reach

agreement with the Vietnamese authorities on such a program. I am concerned, however, that there may be some potential misunderstandings about what intensified collaboration might involve in this case. Specifically, the Board's report to the Interim Committee does not envisage the creation of support groups in every case. For example, it appears that Viet Nam would be able to normalize its relations with creditors and donors without the kind of exceptional arrangements that support groups were created to develop.

Finally, with regard to the proposed decision, I am prepared to offer specific amendments along the lines suggested in my remarks. I can also agree to the amendment of paragraph 3 proposed by Mr. Ismael.

Mr. McCormack said that, like other speakers, he welcomed the progress in recent months made by the Vietnamese authorities, notably the devaluation of the currency. He also welcomed the willingness of the authorities to receive a Fund mission in January to discuss, inter alia, a shadow program. Nevertheless, he had to express, as he had on several occasions in the past, his continued frustration with the failure of Viet Nam to make payments to the Fund. That important point should remain highlighted. He agreed with Mr. Rieffel that payments over the forthcoming months should be made as they fell due. Finally, he agreed with the decision as amended by Mr. Ismael, but he would prefer to leave paragraph 4 as drafted.

The staff representative from the Asian Department remarked that the staff envisaged that the preparation of a comprehensive medium-term program of structural adjustment for Viet Nam would entail the formulation of a policy framework paper. As to the absence of a reference to Alternative II in the staff paper, it should not be interpreted as any slackening of commitment on the part of the authorities to the implementation of a comprehensive adjustment program. Under the framework of both Alternative II and the intensified collaborative approach, the implementation of such a program was a critical initial element in the process.

Regarding the behavior and composition of imports in 1988, the available statistics indicated that total imports from both convertible and nonconvertible areas had increased in volume terms by over 30 percent for fertilizer and by 20 percent for steel, the staff representative reported. Little information was available on the behavior of imports from the convertible area alone, but the authorities indicated that the major increases in such imports were for essential consumer items and raw materials. The flow of imports from the convertible area was constrained by the supply of financing. A substantial amount of the increase in imports from the convertible area in the first nine months of 1988 appeared to reflect the authorities' ability to finance those imports through short-term suppliers' credits, and it was unlikely that such financing would have been available to finance other balance of payments transactions.

A detailed breakdown of debt service payments made to the nonconvertible area was not available, the staff representative noted. However, some information had been provided by the authorities to indicate that during the first nine months of 1988, Viet Nam's current account deficit vis-à-vis the nonconvertible area had amounted to about 950 million transferable rubles, which had been financed by net capital inflows from the nonconvertible area of an equal amount, consisting of gross inflows of almost 1.8 billion transferable rubles and repayments of just over 800 million transferable rubles. Those transactions largely reflected the arrangements for financing Viet Nam's trade with the nonconvertible area; that trade had been financed initially through short-term credits from the International Bank for Economic Cooperation and subsequently refinanced through longer-term bilateral flows from the nonconvertible area.

With respect to payments made to bilateral creditors in the convertible area, the staff had no additional information on the arrangements with Iraq and private banks, the staff representative added.

Replying to a question, the staff representative from the Asian Department said that the Vietnamese authorities had indicated that the blocked accounts in the United States amounted to about \$200 million.

Mr. Ismael commented that his opening statement had attempted to be balanced, reasonable, realistic, and constructive while dispelling any misunderstanding about Viet Nam's intention to normalize its relationship with the Fund. The authorities were reacting to the new collaborative approach by stating their readiness to adopt and implement a comprehensive adjustment program; they had also proposed the release of the funds in the blocked assets in the United States as a realistic means of fully and promptly settling Viet Nam's arrears to the Fund. As a result of those steps, the authorities hoped that the relationship with the Fund would be normalized.

Mr. Rieffel remarked that, with respect to the blocked assets, the approach outlined by Mr. Ismael would not be regarded as particularly constructive by his authorities. He was somewhat concerned that if the discussion were concluded without addressing that question, the authorities might infer an endorsement of their strategy.

Mr. Ismael explained that his authorities had wanted to present a concrete suggestion in the context of the second key element of the intensified collaborative approach. They had proposed the release of the blocked assets, but they would welcome any better solution that would allow the full and prompt settlement of the arrears to the Fund.

Mr. Posthumus stated that the Fund was not responsible for solving the problem of the blocked accounts. It should be made clear that the Fund could not be a party to that dispute and therefore could not accept that proposal as a solution to the arrears problem.

Mr. Ismael said that the Fund should not take a dogmatic approach whereby it would make no effort to resolve the problem of blocked accounts. The authorities' suggestion was preferable to empty commitments to the Board to make full and prompt settlement. Indeed, his authorities had put forward a concrete proposal that should be studied carefully to determine, in response to the new intensified collaborative approach, whether the Fund should intermediate and whether a solution could be found.

The staff representative from the Legal Department noted that the issue of the blocked accounts had arisen repeatedly in the context of the reviews of Viet Nam's overdue obligations to the Fund. On earlier occasions, the Managing Director had contacted the U.S. authorities on the matter, and discussions had been held to clarify the issue from the Fund's point of view. The Fund's policy on payments disputes stated that the Fund's good offices were provided only at the request of both countries in question. The Fund's policy was therefore to remain outside the present case--where claims and counterclaims were involved--as in those cases that were not amenable to settlement by the Executive Board.

Mr. Rieffel suggested that, with respect to the proposed decision, it might be appropriate to refer in paragraph 2 to the Vietnamese authorities' recognition of the Fund's preferred creditor status, as had been done in another case one week previously.

The staff representative from the Legal Department pointed out that while the Vietnamese authorities recognized the Fund's preferred creditor status, that recognition was qualified by the need for essential imports. Therefore, it would be preferable not to include the reference in the decision.

Mr. Rieffel proposed that paragraph 2 could be amended to state that the Fund concluded that Viet Nam had the ability to meet its financial obligations to the Fund as they fell due in the future, and that the Fund urged Viet Nam to resume payments to the Fund in order to demonstrate its willingness to cooperate with the Fund in settling promptly and fully its overdue obligations. Another way of proceeding was to reflect those sentiments in the Managing Director's communication to the authorities summarizing the discussion.

Mr. Goos expressed his concern about including in the decision an explicit statement that the authorities had the ability to meet their obligations as they fell due in the future, implying that they were not able to meet the obligations that had accumulated in the past.

Mr. Jalan commented that making a judgment about the ability of a country to make payments as they fell due in the future or to repay outstanding obligations would be a complicated exercise that would have to take into consideration other factors that were not known to the Board. He urged that that amendment not be included in the decision.

Mr. Enoch said that his chair believed that Viet Nam could do more than meet its future payments as they fell due. He could go along with Mr. Rieffel's suggestion that the Managing Director's communication to Viet Nam state that unless, at a minimum, payments falling due were made over the next month, there would be severe credibility problems about the commitment of the authorities in advance of the Fund's mission to Hanoi in January.

Mr. Legg stated that it would be a good signal if Viet Nam were able to resume payments as they fell due. Nonetheless, that issue should be mentioned in the Managing Director's communication rather than the decision.

Mr. Posthumus said that it would not be appropriate for the Board to establish a precedent whereby a member without a shadow program could pay only amounts as they fell due. To date, within the framework of the cooperative approach, the Board had accepted that procedure only in the case of members with a shadow program.

Mr. Rieffel stated that his observation had been specific to the case of Viet Nam. His authorities had always considered that the country should move immediately to pay whatever amounts possible. In those circumstances where a country was not able to eliminate its arrears completely, his authorities did not consider it appropriate for it to refrain from paying when some payment was possible.

Mr. Al-Assaf said that he would consider a country's payment of obligations as they fell due proof that it was ready to normalize its relations with the Fund and take part in the intensified collaborative approach.

The Acting Chairman said that it would be possible to present the views of Directors on the issue in the communication to the authorities, rather than in the decision, thereby alleviating the concerns expressed by Mr. Goos and others.

Mr. Fogelholm stated that paragraph 2 did not recognize the discrimination against the Fund. A reference to Viet Nam's making payments to other creditors while making none to the Fund would be appropriate.

Mr. Enoch proposed that Mr. Fogelholm's suggestion be met by inserting a clause reading "while Viet Nam has made payments to other creditors" at the end of the first sentence in paragraph 2.

With respect to paragraph 4, it would be helpful to flag explicitly the Board's forthcoming discussion on the Fund's policies on arrears, Mr. Enoch commented. He therefore suggested that a new sentence be inserted to that effect at the beginning of the paragraph, followed by a sentence stating that the Fund would review the matter of Viet Nam's overdue financial obligations to the Fund within three months from the

date of the present decision in the light of those discussions and in the light of actions taken by Viet Nam in the meantime.

Mr. Al-Assaf, Mr. McCormack, and Mr. Rieffel said that they supported Mr. Enoch's proposals.

The Executive Board then took the following decision:

1. The Fund has reviewed further the matter of Viet Nam's continuing failure to fulfill its financial obligations to the Fund in light of the facts and developments described in EBS/88/246 (11/30/88).

2. The Fund notes that only modest payments have been received since 1985 and that no payment has been received from Viet Nam since May 1988, while Viet Nam has made payments to other creditors. The Fund deeply regrets the continuing failure of Viet Nam to settle its arrears to the Fund, which are placing a financial burden upon other members and reducing Fund resources needed to help others. The Fund again urges Viet Nam to make prompt and full settlement of its overdue obligations to the Fund and stresses that settlement of these arrears should be given the highest priority.

3. The Fund welcomes the economic reform measures implemented recently by Viet Nam and its desire to adopt and implement a comprehensive and realistic adjustment program aimed at achieving sustained economic growth and balance of payments viability. The Fund also welcomes the authorities' desire to pursue an intensified collaborative approach toward the elimination of Viet Nam's arrears to the Fund and expresses its continued readiness to assist Viet Nam in the formulation of a comprehensive adjustment program as a critical step in this approach.

4. The Fund will shortly be discussing its policies on arrears to the Fund. It will review the matter of Viet Nam's overdue financial obligations to the Fund again within three months from the date of this decision, in the light of these discussions and of the actions taken by Viet Nam in the meantime to settle its arrears to the Fund and to adopt and begin implementing a comprehensive adjustment program.

Decision No. 9037-(88/175), adopted
December 7, 1988

APPROVED: June 13, 1989

LEO VAN HOUTVEN
Secretary

