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AGENDA

EBS/87/122

CONFIDENTIAL

June 5, 1987

To: Members of the Executive Board

From: The Secretary

Subject: Somalia - Request for Stand-By Arrangement and Request for  
Arrangements Under the Structural Adjustment Facility

With the establishment of Italy's voluntary contribution account, and the payments already received from Somalia, the Fund now appears to have firm assurances that Somalia will shortly clear its overdue financial obligations to the Fund. It therefore seems appropriate in these special circumstances to issue Somalia's policy framework paper as well as the paper on Somalia's request for a stand-by arrangement equivalent to SDR 33.15 million, and for arrangements under the structural adjustment facility. This subject is expected to be scheduled for discussion by the Executive Board on Wednesday, June 17, 1987. Draft decisions will be circulated when the arrears are cleared.

Mr. Jimenéz (ext. 6952) or Mr. Scheuer (ext. 6940) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

Att: (1)



INTERNATIONAL MONETARY FUND

SOMALIA

Requests for Stand-By Arrangement and for Arrangements under the  
Structural Adjustment Facility

Prepared by the African Department and the Exchange  
and Trade Relations Department

(In consultation with the Fiscal Affairs and  
Legal Departments)

Approved by A.D. Ouattara and W.A. Beveridge

June 5, 1987

I. Introduction

In the attached letter dated June 5, 1987, the Government of Somalia requests a 20-month stand-by arrangement in an amount equivalent to SDR 33.15 million, 75.0 percent of Somalia's quota, representing an annual access of 45 percent of quota. In addition, the Government of Somalia requests a three-year structural adjustment arrangement and the first annual arrangement under the structural adjustment facility (SAF). The amount that will be available to Somalia under the SAF is currently projected at about SDR 20.774 million, and the first loan thereunder is for the amount of SDR 8.84 million (Table 1).

At the end of April 1987, Fund holdings of Somali shillings subject to repurchase were SDR 118.73 million (268.6 percent of quota). Overdue obligations totaled SDR 17.77 million. The proposed access under the stand-by arrangement would reduce the Fund's holdings of Somali shillings subject to repurchase to SDR 108.83 million (246.2 percent of quota) by the end of 1988, given the schedule of repurchases and assuming all purchases are made. Purchases under the proposed arrangement will be divided into six equal installments, with the first one available on Fund approval of the program. The proposed arrangement would be financed in the ratio of 1 to 2 from ordinary and borrowed resources. 1/

The access of 45 percent was deemed necessary in order for the Fund to play a meaningful catalytic role in obtaining financial support for

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1/ Available borrowed resources arranged under the enlarged access policy presently consist of amounts borrowed from Saudi Arabia under agreements with the Saudi Arabian Monetary Agency; borrowed resources have also become available under the December 1986 borrowing agreement with the Government of Japan.

Table 1. Somalia: Use of Fund Credit, 1987-88

	Outstanding April 30, 1987	1987			1988			
		May- June	July- Sept.	Oct.- Dec.	Jan.- March	April- June	July- Sept.	Oct.- Dec.
<u>(In millions of SDRs)</u>								
Total transactions (net)		-1.52	-0.39	-0.14	1.25	-3.40	-2.61	-3.87
Transactions under tranche policies (net)		-10.36	-0.39	-0.14	1.25	-5.29	1.46	0.21
Purchases		5.53	5.53	5.53	5.53	--	5.53	5.53
Ordinary resources		(1.84)	(1.84)	(1.84)	(1.84)	(--)	(1.84)	(1.84)
Borrowed resources		(3.68)	(3.68)	(3.68)	(3.68)	(--)	(3.68)	(3.68)
Repurchases		15.89	5.14	5.67	4.28	5.29	4.06	5.32
Ordinary resources		(0.37)	(1.33)	(0.47)	(0.47)	(0.13)	(0.13)	(0.13)
Borrowed resources		(3.36)	(3.81)	(5.19)	(3.80)	(5.17)	(3.94)	(5.19)
Arrears <sup>1/</sup>		(12.16)	(--)	(--)	(--)	(--)	(--)	(--)
Transactions under special facilities (net)		8.84	--	--	--	1.89	-4.08	-4.08
CFF repurchases		--	--	--	--	(-4.08)	(-4.08)	(-4.08)
SAF loans		(8.84)	(--)	(--)	(--)	(-5.97)	(--)	(--)
Total Fund credit outstanding	118.73	117.21	117.60	117.46	118.71	115.31	112.70	108.83
Under tranche policies	(86.13)	(75.7)	(76.16)	(76.02)	(77.27)	(71.98)	(73.44)	(73.65)
Under special facilities	(32.60)	(41.44)	(41.44)	(41.44)	(41.44)	(49.33)	(39.26)	(35.18)
<u>Memorandum items:</u>								
Trust Fund loans (net)		-2.03	-2.12	-3.10	-3.19	-4.16	-4.25	-5.22
<u>(In percent of quota)</u>								
Total Fund credit outstanding	268.63	265.18	266.06	265.57	268.57	260.88	254.97	246.22
Under tranche policies	(194.87)	(171.43)	(172.30)	(171.98)	(174.81)	(162.84)	(166.15)	(166.62)
Under special facilities	(73.76)	(93.76)	(93.76)	(93.76)	(93.76)	(98.04)	(88.82)	(79.60)

Sources: IMF, Treasurer's Department; and staff estimates.

<sup>1/</sup> Arrears of repurchases with respect to purchases only.

Somalia during the program period and to support the important modifications in the external sector envisaged under the program.

Somalia has been overdue in its financial obligations to the Fund during most of the past two years, and complaints under Rules K-1 and S-1 were issued on October 25, 1985 and a notice of failure to settle Trust Fund obligations was issued on December 6, 1985. The complaint under Rule K-1 and the notice were withdrawn following full settlement of Somalia's overdue financial obligation to the Fund on April 22, 1986. A second and a third complaint under Rule K-1 and notice of failure to settle a Trust Fund obligation were issued on July 22, 1986, and February 2, 1987, while a complaint under Rule S-1 was made on April 7, 1987. The complaints and notices were withdrawn after Somalia settled all its overdue financial obligations to the Fund.

The Somali authorities have prepared, in close collaboration with the staffs of the Fund and the World Bank, a policy framework paper setting forth the Government's basic economic objectives for the three-year period 1987-89 and the macroeconomic and structural adjustment policies designed to achieve these objectives. This paper, dated June 5, 1987, has been transmitted to the Managing Director of the Fund and the President of the World Bank, and it is expected to be considered by the Bank's Executive Directors at a meeting of the Committee of the Whole, in the first half of June.

During 1981-83, Somalia undertook policy reforms within the framework of Fund-supported programs and made substantial progress toward improving resource allocation and reducing financial imbalances. During this period, the country moved from a highly controlled economic system toward market orientation. Most price and other controls were removed, producer prices were adjusted to provide incentives, a reassessment and reform of the public enterprises was begun, the exchange rate was devalued, and the exchange system was liberalized. At the same time, demand-management policies were tightened significantly.

Somalia's improved economic performance was interrupted in 1984. Total exports fell by about 55 percent, owing to the full-year impact of the ban on Somali cattle imports in a major market, which began in 1983. In addition, the grace period on a large number of loans expired, and Somalia faced a debt service ratio of 57 percent in 1984 (US\$107 million), compared with only 18 percent (US\$30 million in 1983). The impact of these factors was aggravated by a major weakening of financial policies. The overall budget deficit reached 8.1 percent of GDP, with almost half of the deficit financed by the banking system. Inflation was rekindled, with the cost of living rising by 82 percent, leading to the re-emergence of price and cost distortions.

In 1985 the authorities once again embarked on a stabilization program supported by a stand-by arrangement, aimed at reducing the large internal and external imbalances that had reappeared, and at furthering the structural reform of the economy. Despite the extension of the time

period of the stand-by arrangement, not all of the program's objectives were attained. Growth in 1985-86 was above the program's targets, reaching an average of over 5.6 percent per year, compared with a target of 4.0 percent per year, partly as a result of good weather conditions (Table 2). However, the failure to implement several economic measures, and delays in the flow of foreign assistance, led to more expansionary financial policies than programmed. In 1985, total domestic credit rose by 29 percent of the initial money stock and broad money by 45 percent, compared with targets of 7 percent and 17 percent, respectively. Expansion of the money stock averaged about 31 percent per annum, compared with a target of 21 percent. In 1985 both the private and the government sectors were recipients of the large credit expansion. The overall budgetary deficit (commitment basis) of central government operations including grants was 6.2 percent of GDP, compared with a target of 2.0 percent; domestic financing of the budget reached 1.1 percent of GDP; excluding grants the budget deficit reached 13.1 percent, compared with a target of 8.9 percent. Developments in 1986 indicated a substantial tightening of financial policies through the last testing date of the arrangement (July) and a major reversal in the rest of the year. The growth of net domestic credit reached 25 percent of the initial money stock, compared with a target of 9.7 percent. Broad money expanded by 37 percent as opposed to a target of 12 percent. Contrary to the previous year, the expansion of credit was largely directed to the public enterprises. Net credit to the Government expanded by only about 7 percent of the initial broad money stock. The overall deficit (including grants) of government operations rose slightly to 6.6 percent of GDP (14.2 percent excluding grants) as an improved revenue performance and additional foreign grants were largely offset by increased government expenditure. However, arrears on debt service equivalent to about 2 percent of GDP were incurred and the resulting cash financing requirement (4.6 percent of GDP) was entirely met through foreign financing.

In 1985-86 the balance of payments continued to show large imbalances, while the exchange rate in the free market depreciated by an annual average of 25 percent. Despite enhanced donor support, there have been large shortfalls in cash assistance. Cash flow problems emerged when the assistance was not disbursed on schedule to the detriment of the financial program. Nevertheless, the external current account deficit, including grants (as measured by the exchange rate necessary to maintain the purchasing power parity at the 1973 level), has shown continuous adjustment, falling from about 14 percent of GDP in 1984 to 7.1 percent in 1986. Measured at the average official rate, however, there was a small increase from about 4.5 percent in 1984 to 5.3 percent in 1986. The program had targeted a reduction of about 2 percentage points in the current account balance as measured by the constant purchasing power parity exchange rate, compared with the actual 7 percentage point adjustment which took place. The adjustment was

Table 2. Somalia: Selected Economic and Financial Indicators, 1982-90

	1982	1983	1984 <u>1/</u>	1985 <u>2/</u> Prog.	1985 <u>3/</u> Prel. act.	1986 <u>4/</u> Prog.	1986 Rev. est.	1987 Prog.	1988 Prog.	1989 Prog.	1990 Prog.
(Growth rate in percent, unless otherwise specified)											
National income and prices											
GDP at constant factor cost	8.5	2.4	3.5	4.0	6.4	4.0	5.0	4.1	4.1	4.1	4.1
Consumer price index December/December	34.0	48.9	82.0	20.0	30.5	22.0	30.7	22.0	15.0	9.0	7.0
Trends in central government finance											
Revenue	22.0	54.1	-6.4	92.9	31.2	59.0	82.0	33.7	40.0	27.6	16.8
Total revenue and grants	41.4	40.4	11.2	121.7	98.7	66.7	68.2	10.4	11.2	16.9	14.0
Total expenditure	44.2	23.7	69.7	43.3	58.5	59.0	62.8	74.6	12.6	11.6	9.8
Investment expenditure	72.7	-22.0	62.7	...	154.2	...	61.6	155.7	6.8	8.4	11.4
Trends in monetary aggregates <u>5/</u>											
Net domestic credit	10.9	4.7	81.4	6.7	29.0	9.7	25.1	7.3	...	...	...
Government (net)	-3.4	-5.9	48.1	0.6	15.9	-0.6	6.9	-3.8	...	...	...
Private	14.3	10.6	33.3	6.0	13.1	10.3	18.2	11.1	...	...	...
Broad money	14.4	7.1	22.4	17.4	45.4	12.4	37.0	13.1	...	...	...
Counterpart funds	...	...	...	1.4	2.1	...	8.6	...	...	...	...
Residents' foreign currency deposits	...	...	...	1.0	27.8	...	1.1	...	...	...	...
Velocity	4.9	6.4	9.9	...	10.1	...	11.5	...	...	...	...
Interest rates											
Commercial bank lending rate											
Minimum	12.0	12.0	12.0	15.0	15.0	19.0	15.0	... <u>6/</u>	... <u>6/</u>	... <u>6/</u>	... <u>6/</u>
Maximum	14.5	14.5	14.5	20.0	21.0	24.0	22.0	... <u>6/</u>	... <u>6/</u>	... <u>6/</u>	... <u>6/</u>
Commercial bank deposit rate											
Ordinary savings	8.0	8.0	8.0	...	12.0	...	12.0	14.0	14.0	14.0	14.0
12-month time deposits	9.5	9.5	9.5	...	16.0	...	18.0	20.0	20.0	20.0	20.0
Maximum	11.0	11.0	11.0	18.0	18.0	22.0	24.0	24.0	24.0	24.0	24.0
Trends in external sector (in U.S. dollars)											
Exports, f.o.b.	20.2	-27.0	-38.0	81.7	50.0	21.5	6.5	16.2	13.9	11.5	10.3
Imports, c.i.f.	14.7	-7.0	-9.8	24.7	-9.3	6.3	-1.1	11.2	10.5	1.3	5.3
Normal effective exchange rate (depreciation -)	-27.5	-10.9	-8.1	...	-56.8	...	-48.2	...	...	...	...
Real effective exchange rate (depreciation -)	-19.6	10.5	59.6	...	-44.8	...	-34.1	...	...	...	...
(In percent of GDP)											
Overall budget balance											
Including grants	-6.3	-3.7	-8.1	-2.0	-6.2	-6.0	-6.6	-6.0	-5.7	-4.6	-3.7
Excluding grants	-10.6	-6.9	-11.2	-8.9	-13.1	-13.8	-14.2	-22.4	-19.0	-17.2	-16.2
Balance of payments											
Current account balance <u>7/</u>	-10.2	-13.3	-14.0	-10.0	-9.2	-11.8	-7.1	-3.8	-6.3	-4.9	-4.3
Current account balance <u>8/</u>	-5.7	-6.8	-4.5	...	-4.3	...	-5.3	-4.4	-7.4	-5.9	-5.3
Current account balance, excluding grants <u>7/</u>	-22.3	-26.6	-30.8	-30.6	-27.3	-24.2	-20.7	-20.2	-19.9	-17.3	-16.2
Current account balance, excluding grants <u>2/</u>	-12.6	-13.6	-9.8	...	-12.7	...	-15.5	-23.9	-23.4	-21.0	-20.1
Overall balance <u>5/</u>	-3.4	-7.8	-13.4	-2.8	-4.4	-8.2	-6.1	0.3	-1.6	-0.5	0.4
Overall balance <u>8/</u>	-1.9	-4.0	-4.3	...	-2.0	...	-4.5	0.4	-1.9	-0.6	0.4
(In millions of U.S. dollars unless otherwise specified)											
Current account balance	-131.0	-147.0	-145.0	-131.0	-104.0	-169.0	-102.0	-58.0	-105.0	-88.0	-83.0
Current account, excluding grants	-288.0	-295.0	-319.0	-400.0	-309.0	-347.0	-297.0	-313.0	-331.0	-311.0	-315.0
Overall balance of payments	-44.0	-86.0	-139.0	-37.0	-50.0	-117.0	-87.0	5.0	-27.0	-9.0	7.0
Gross official reserves	14.3	15.8	6.3	39.0	11.6	12.0	26.6	34.6	40.9	44.8	49.9
External debt, including IMF	856.2	958.5	1,023.3	1,446.8	1,229.7	1,872.0	1,338.0	1,399.0	1,465.0	1,493.0	1,552.0
Debt service ratio <u>9/</u>	...	...	57.0	27.2	68.0	74.8	93.2	97.2	90.7	68.5	52.3
External payments arrears <u>10/</u>	55.6	82.8	117.8	—	67.0	28.4	143.1	57.0	21.0	—	—
External commercial arrears	...	...	33.0	10.0	16.1	0.2	9.5	1.5	—	—	—

Sources: Data provided by the Somali authorities; and staff estimates. GDP estimates are based on data provided by the Somali authorities, and staff estimates, and differ from estimates shown in S/86/213 (1986 Recent Economic Developments).

1/ Balance of payments data for interest and amortization payments, as well as debt service ratio, are on an accrual basis.

2/ ERS/86/93.

3/ The fiscal and monetary data include the resources accruing from the gap-fill exercise.

4/ S/86/225.

5/ Change in relation to broad money at the beginning of the year. Beginning with 1985 estimates, broad money excludes foreign currency deposits and counterpart fund deposits.

6/ Lending rates to be based on the cost of funds.

7/ GDP in Somali shillings converted to U.S. dollars at rates necessary to maintain the purchasing power parity at 1973 level.

8/ GDP in Somali shillings converted to U.S. dollars at the average official rate.

9/ Accrual basis; data not available for 1982-83.

10/ End of period.

largely reflected in reduced imports. As an average, imports were 8 percent below the target in 1985-86. The smaller export and other current account earnings resulted in a lower availability of foreign exchange for free market imports, and the reduced level of foreign assistance led to a lower level of official imports. The overall deficit fell to US\$50 million in 1985, from US\$139 million in 1984; it expanded somewhat in 1986, reaching US\$87 million. In 1985 the balance of payments was largely financed by debt relief and by drawings on the Fund. There was also a large net repayment of arrears through cash payments and debt relief. In 1986 the balance of payments was largely financed by an increase in debt service arrears.

At the end of 1984, external arrears, mainly for debt service payments, totaled US\$117.8 million. In the course of 1985, through debt rescheduling and repayments, there was a large liquidation of arrears, but new arrears emerged during the year. On December 31, 1985, arrears totaled US\$67.0 million. During 1986 the authorities were unable to arrange for a Paris Club meeting because a stand-by arrangement with the Fund did not cover the full calendar year and new arrears were accumulated, including on the Paris Club special account set up following the 1985 rescheduling. At the end of 1986, total external arrears reached US\$143.1 million (Appendix Table I). Somalia's debt service ratio reached 93 percent in 1986 compared with 68 percent in 1985. The ratio is expected to remain high in the medium term, estimated at 91 percent in 1987, 88 percent in 1988 and 83 percent in 1989. The decline largely results from the heavy concentration of obligations due to the Arab Monetary Fund and the IMF during this period (Appendix Table II).

Since the beginning of 1985, the exchange rate system in Somalia has undergone significant modifications. The average exchange rate recorded a large depreciation and there has been a convergence of the free market, the official, and the auction exchange rates. The ratio of the free market rate to the official rate fell from about 3.5 in December 1984 to 2.7 in December 1985, but narrowed significantly in 1986 and ended the year at 1.5. Through April 1987, it widened slightly to 1.7 (Table 3). Beginning on September 1, 1986, an auction for imports was initiated with the support of the World Bank and some bilateral donors. The auction, which is held twice a month, helped stabilize the exchange rate in the free market by providing an indication to the private sector of a regular availability of foreign exchange. The auction rate has continued to have a small discount when compared with the free market rate.

## II. Elements of the Program

Despite some positive results from the previous stabilization program, Somalia continues to face serious internal and external imbalances. Financial policies have been more expansionary than programmed, and inflation remains high and continues to distort costs



Table 3. Somalia: Exchange Rates, 1984-87 <sup>1/</sup>

(In Somali shillings per U.S. dollar)

		Official rate	Commercial bank rate <u>2/</u>	Free market rate <u>3/</u>	Auction rate <u>4/</u>	Effective export rate <u>5/</u>	Ratio of free market rate to		
							Official rate	Auction rate	Effective export rate
1984	Dec.	26.0	...	80-100 <u>6/</u>	...	26.0	3.5	...	3.5
1985	Jan.	36.0	80.4	89.0	...	70.5	2.5	...	1.3
	Feb.	36.5	81.2	89.4	...	70.9	2.4	...	1.3
	March	37.0	82.0	91.4	...	72.4	2.5	...	1.3
	April	37.0	84.4	92.6	...	73.1	2.5	...	1.3
	May	40.1	84.4	93.8	...	75.0	2.3	...	1.3
	June	40.6	84.4	97.8	...	77.8	2.4	...	1.3
	July	40.6	84.4	101.5	...	80.2	2.5	...	1.3
	Aug.	40.6	84.4	100.2	...	80.6	2.5	...	1.3
	Sept.	40.6	84.4	100.7	...	79.7	2.6	...	1.3
	Oct.	40.6	84.4	107.2	...	83.9	2.5	...	1.3
	Nov.	42.5	84.4	110.5	...	86.7	2.6	...	1.3
	Dec.	42.5	84.4	114.7	...	89.4	2.7	...	1.3
1986	Jan.	54.5	84.4	114.8	...	93.7	2.1	...	1.2
	Feb.	54.5	84.4	122.9	...	99.0	2.3	...	1.2
	March	58.5	84.4	138.6	...	110.6	2.4	...	1.3
	April	62.5	84.4	148.1	...	118.1	2.4	...	1.3
	May	66.5	84.4	152.9	...	122.7	2.3	...	1.2
	June	70.5	84.4	154.0	...	124.8	2.2	...	1.2
	July	74.5	84.4	150.8	...	124.1	2.0	...	1.2
	Aug.	78.5	84.4	138.9	...	117.8	1.8	...	1.2
	Sept.	82.5	84.4	138.4	100.0 <u>7/</u>	118.8	1.7	...	1.2
	Oct.	86.5	...	139.7	96.5 <u>8/</u>	121.1	1.6	1.4	1.2
	Nov.	90.5	...	136.9	105.5 <u>9/</u>	120.7	1.5	1.3	1.1
	Dec.	90.5	...	139.5	122.3 <u>10/</u>	122.4	1.5	1.1	1.1
1987	Jan.	90.5	...	156.4	125.4 <u>11/</u>	133.3	1.7	1.2	1.2
	Feb.	90.5	...	149.2	118.7 <u>12/</u>	128.7	1.6	1.3	1.2
	March	90.5	...	152.9	123.0 <u>13/</u>	131.1	1.7	1.2	1.2
	April	90.5	...	155.8 <u>14/</u>	128.9 <u>15/</u>	132.9	1.7	1.2	1.2

Source: Data provided by the Somali authorities.

- <sup>1/</sup> End of period except where otherwise specified.
- <sup>2/</sup> Unified with official rate in October 1986.
- <sup>3/</sup> Monthly transactions weighted average of import, export, and external account rates.
- <sup>4/</sup> Weighted average auction rate on day nearest end of month.
- <sup>5/</sup> Weighted average exchange rate resulting from surrender requirements.
- <sup>6/</sup> Parallel rate. Actual exchange rate dependent on quantity exchanged.
- <sup>7/</sup> October 1 auction.
- <sup>8/</sup> November 1 auction.
- <sup>9/</sup> December 1 auction.
- <sup>10/</sup> January 3 auction.
- <sup>11/</sup> February 3 auction.
- <sup>12/</sup> March 1 auction.
- <sup>13/</sup> April 1 auction.
- <sup>14/</sup> Through April 15.
- <sup>15/</sup> April 16 auction.

and prices. In addition, Somalia faces large, but declining financing gaps in its external accounts. The authorities recognize that a strengthening of policies is required, but, given the magnitude of the imbalances, they feel the problems must be resolved in a medium-term framework that contains supply-side measures that lay the foundation for a more sustained development effort. In implementing these policies, Somalia faces many serious disadvantages: it has a limited resource base, extremely scarce trained manpower, and a fragile ecology, which could be unbalanced by the overutilization of the rangelands. In addition, the country ranks low in terms of social indicators (Appendix Table III). The population is estimated to be growing in excess of 3 percent per annum, but the urban population is projected to be increasing in excess of 5 percent per annum.

Somalia's program addresses its problems in the context of the medium-term framework and requires continued generous donor support over a number of years. However, even with the full implementation of the policies described below, in combination with generous aid, there are inherent structural bottlenecks which limit the speed at which the structural limitation to development can be overcome. There are no quick fixes to Somalia's present development problems, and perseverance in policy implementation over a number of years will be required.

#### 1. Objectives

The Government's medium-term development strategy consists of three main objectives: (i) stabilization in the short term; (ii) medium-term adjustment with growth; and (iii) the laying of the foundations for sustainable long-term economic and social development. However, the latter two objectives depend on the successful implementation of stabilization policies.

To attain these objectives, the program aims at achieving a growth of real domestic product of at least 4 percent over the period 1987-89, while maintaining the real level of per capita private consumption and increasing private savings and investment. Gross domestic expenditure has been reduced substantially in 1986 from 1983-84 with both private and public consumption falling (Table 4). This trend is expected to continue, on the basis of the stabilization policies which target a reduction of public sector consumption. The ratio of private consumption will fall on the basis of the stabilization policies, especially wage restraints and increased taxation. A key element, however, is to maintain the level of real private consumption. The new measures in the exchange system, the continued liberalization of the production sector, and the emphasis on market prices are providing increased investment opportunities in the private sector, which will lead to an increasing ratio of investment to GDP. Credit policy will support this objective.

The program targets a reduction of inflation over the three-year period. The growth in the cost of living index is expected to fall to

Table 4. Somalia: Expenditure on Gross Domestic Product  
at Current Market Prices, 1979-90

(In percent of gross domestic product)

	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990
Gross domestic expenditure	130.8	131.7	122.3	125.2	130.8	133.5	125.4	119.0	122.3	122.2	120.5	120.1
Consumption	108.3	114.3	94.8	98.6	114.3	113.8	103.5	102.1	99.5	98.9	98.2	97.4
Public	19.4	14.6	12.1	11.8	13.7	11.7	9.1	9.4	7.8	8.3	8.7	8.4
Private	88.9	99.7	82.7	86.8	100.5	102.1	94.4	92.7	91.6	90.6	89.5	89.0
Domestic investment	22.6	17.4	27.5	26.6	16.6	19.7	21.9	16.9	22.9	23.3	22.3	22.6
Gross fixed investment	28.6	21.9	18.0	19.9	13.4	18.0	20.5	15.4	22.4	22.8	21.8	22.1
Public	27.1	20.0	16.6	17.7	11.0	15.1	17.7	12.4	19.3	16.9	15.9	15.8
Private	1.5	1.9	1.4	2.2	2.4	2.9	2.6	3.0	3.1	5.9	5.9	6.4
Change in stocks (private)	-6.0	-4.5	9.5	6.7	3.2	1.8	1.3	1.5	0.5	0.5	0.5	0.5
Resource balance	-30.5	-31.7	-22.3	-25.2	-30.8	-33.5	-25.4	-19.0	-22.3	-22.2	-20.5	-20.1
Exports	10.8	19.0	12.7	15.6	15.5	11.1	12.5	8.5	10.6	10.9	11.5	12.0
Goods	10.8	12.7	8.3	10.6	9.0	6.0	8.2	6.9	8.8	9.2	9.8	10.3
Nonfactor services	--	6.3	4.4	5.0	6.5	5.1	4.2	1.6	1.8	1.7	1.7	1.7
Imports	-41.7	-50.7	-35.0	-40.8	-46.3	-44.6	-37.9	-27.5	-32.9	-33.2	-32.0	-32.1
Goods	-40.2	-43.7	-30.9	-37.5	-40.6	-39.2	-32.4	-25.3	-30.9	-31.5	-30.4	-30.5
Nonfactor services	-1.4	-6.9	-4.1	-3.3	-5.7	-5.4	-5.5	-2.2	-2.0	-1.7	-1.6	-1.6
GDP at market prices	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Sources: Somali authorities; World Bank; and Fund staff estimates.

22 percent in 1987, to about 15 percent in 1988, and to under 10 percent in 1989.

The Government intends to reduce the overall budgetary deficit gradually over the period 1987-89. In 1987 the overall budgetary deficit (including grants) is targeted at 6 percent of GDP, compared with 6.6 percent in 1986, but it is expected to fall to 4.6 percent by 1989. Excluding grants, the deficit is set at 22.4 percent in 1987, but it is projected to fall to 17.2 percent by 1989. In addition, the Government will be making net repayments of its domestic debt. In 1987 this will total 0.3 percent of GDP. The clearing of arrears on external debt payments of US\$17.6 million is projected in 1987. A falling financing gap in government operations is projected through 1989 which will be met through debt relief.

The objective in the external sector is the attainment of viability in the balance of payments over the medium term through a reduction of the external current account deficit, a regularization of debt service payments, and reduction of arrears. Below is a description of the policies that will be implemented to attain the objectives previously described. The exposition is divided into two general sections: elements of stabilization and structural adjustment measures. A summary of the financial program is included in Table 5.

a. Elements of stabilization

(1) The exchange system and external targets

Consolidating the gains achieved in the external sector is one of the principal aims of the program. This will be brought about by a further unification of the exchange system, under a liberal trade and exchange regime. Through the efforts made by the Government at unifying the system in 1985 and 1986, the divergence of the exchange rates has been substantially reduced, with most international transactions being carried out at market-determined rates. The successful launching of the auction system in September 1986 was significant in attaining the present position. The auctions have been carried out in a transparent and orderly manner. As a result, the degree of participation in the auctions has increased. The success and acceptance of the auction system by the private sector has led the Government to choose to unify the exchange system through an enhancement of the auction system. Beginning in June, an enhanced auction (based on the Dutch system) will be launched which will absorb the transactions being carried out in the free market and the official market. For a short period of time, petroleum product imports (excluding grants) will continue to be denominated at a special petroleum accounting rate, equal to So. Sh. 105 per U.S. dollar. However, petroleum products will be priced domestically at import parity based on the auction rate. A main auction will be held for import letters of credit open to all importers while a smaller auction, funded by remittances, will be provided for financing service payment needs of residents. A proportion of the latter

Table 5. Somalia: Summary of 1987 Financial Program

<u>Objectives</u>	<u>Status</u>
<ol style="list-style-type: none"> <li>1. Achieve growth of real gross domestic product of at least 4.0 percent.</li> <li>2. Reduce the rate of inflation to about 22 percent by the end of 1987.</li> <li>3. Reduce the overall budgetary deficit (including grants) to 6.0 percent of GDP from 6.6 percent in 1986. Reduce net domestic indebtedness by 0.3 percent of GDP.</li> <li>4. Limit the expansion of net domestic credit to 6.8 percent in 1987, and the growth of broad money to 13.1 percent.</li> <li>5. Viability of the balance of payments over the medium term through a reduction of external current account deficit, and a regularization of external debt payments and a reduction of arrears.</li> </ol>	
<u>Policy measures</u>	<u>Implementation</u>
<ol style="list-style-type: none"> <li>1. <u>External sector policy</u></li> </ol>	
<ol style="list-style-type: none"> <li>a. Adopt an enhanced foreign exchange auction, with the auction rate applicable to all transactions with the exception of imports of petroleum, to which a separate accounting rate may be applied until December 31, 1987. Adopt a 100 percent surrender requirement, at the auction rate, for export proceeds.</li> </ol>	<ol style="list-style-type: none"> <li>a. Being implemented.</li> </ol>
<ol style="list-style-type: none"> <li>2. <u>Fiscal policy</u></li> </ol>	
<ol style="list-style-type: none"> <li>a. Any local currency counterpart of foreign assistance programs in excess of the budgeted amount (So. Sh. 10.5 billion) will be deposited with the banking system and be subject to a 100 percent reserve requirement to be held in an escrow account.</li> </ol>	<ol style="list-style-type: none"> <li>a. Subject to review in July. If there are counterpart Fund resources in excess of the budgeted amount, reductions will be sought in net domestic indebtedness.</li> </ol>
<ol style="list-style-type: none"> <li>b. Undertake a review of the tax system aimed at improving the efficiency of the tax system and increasing the ratio of revenue to GDP.</li> </ol>	<ol style="list-style-type: none"> <li>b. Some earlier studies are already available, and these will be reviewed to develop an agenda for tax reform beginning in 1988.</li> </ol>
<ol style="list-style-type: none"> <li>c. Complete negotiations with Compagnie Général de Surveillance (CGS) on a contract through which the customs service will be provided with a list of minimum sales prices, for the most important exports, on a periodic basis. Review tariffs with the objective of raising at least an additional So.Sh. 100 million in the second half of 1987.</li> </ol>	<ol style="list-style-type: none"> <li>c. Being implemented. These measures are expected to raise revenue by about 0.4 percent of GDP in 1987.</li> </ol>

Table 5. Somalia: Summary of 1987 Financial Program (concluded)

<u>Policy measures</u>	<u>Implementation</u>
d. Strengthen expenditure control by limiting payments by the Central Bank on behalf of the Government to those which have a duly authorized voucher that has been passed through the office of the Accountant General.	d.
e. A review of ordinary expenditure will be held quarterly, with the assistance of the Fund's Resident Representative, to ascertain that expenditures do not exceed the targeted level.	e.
f. Establish a program of action on civil service reform.	f. Discussions with donors interested in supporting the program are continuing.
3. <u>Monetary policy</u>	
a. Reduce net credit to the Government by 8.2 percent.	a. Being implemented. If revenue collections and counterpart funds for external assistance programs exceed the budgeted amount, monetary policy may be tighter than indicated.
b. Increase all domestic currency time and savings deposit rates, with the exception of the current maximum rate, by 2 percentage points.	b. To be implemented.
4. <u>Public enterprises and other sectoral policies</u>	
a. Agree with the World Bank on the number of enterprises whose operations are to be reviewed, and on a time frame for carrying out these reviews.	a. A Bank mission will be going to Somalia in the near future to begin developing a program for review of public enterprise operations.
b. Review the operations of the fishing subsector and the fishing parastatal (Somalfish), with a view to increasing commercial operations and strengthening the development program, particularly to promote private sector activities.	b. To be implemented.
c. Provide the World Bank, by June 30, 1987, a plan of action to promote production, improve marketing, and increase exports of hides and skins.	c. Being implemented, as agreed under the ASAP IDA credit.

resources could be purchased by the commercial bank at the weighted average rate of successful bids for resale for service payments between auctions.

In order to finance the main auction, a 100 percent surrender requirement on exports will be instituted. The main auction will be funded by up to 50 percent of export proceeds with cash and commodity assistance being provided by some donors. The remainder of the export proceeds will be utilized for debt service payments and other official purposes, but will be transacted at the current auction rate.

Holders of external accounts at the Commercial Bank may continue to credit them with inward remittances and to use the proceeds for their own purposes. However, transfers between external accounts will no longer be permitted, and to convert these resources to shillings, holders will have to go through the auction or to sell them to the Commercial Bank at the previous auction rate; thereby providing additional resources for the auction.

Holders of export-promoting and import accounts will be allowed to continue to use the balances in these accounts for imports, but they will not be able to add to their accounts as from the date of the announcement of the enhanced auction.

On a periodic basis, the Government will be reviewing the export surrender values for livestock to ascertain that they reflect market conditions. This will encourage the prompt repatriation of export earnings and their utilization in the auction system.

The auction system and developments in the external sector will be subject to a review with the Managing Director in July 1987. An early review of developments is warranted, given the major changes that are being introduced in the auction system.

The market determination of the rate, within a system of liberal trade and exchange policies, will be an important element in helping the external sector adjust. The key targets in these adjustments are increasing exports by an annual rate of about 13 percent per year between 1986 and 1990; a containment of import growth, with a better allocation of imports; a restructuring of Somalia's external debt payments to reduce the presently high debt service ratio, and the attainment of additional assistance in cash form from donors (Table 6). The latter is important, not only in closing the projected financing gap in the balance of payments, but also in allowing Somalia to regularize its debt position with multilateral organizations, thereby permitting these entities to continue with their lending programs, which have been stalled recently as a result of the built-up arrears. Success in attaining these objectives will result in a gradual narrowing of the external current account balance, both including and excluding grants, a closing of the financing gap in the balance of payments, and a gradual attainment of external viability. The current imbalances in

Table 6. Somalia: Balance of Payments 1984-92

(In millions of U.S. dollars)

	1984	1985	1986 Prel.	1987 Prog. 1/	Projections 1/				
					1988	1989	1990	1991	1992
Current account	-145	-104	-102	-58	-105	-88	-83	-78	-75
Trade balance	-344	-274	-264	-289	-315	-306	-315	-324	-334
Exports, f.o.b.	62	93	99	115	131	146	161	178	196
Livestock	(33)	(66)	(63)	(70)	(77)	(85)	(93)	(102)	(111)
Bananas	(14)	(13)	(17)	(23)	(29)	(32)	(35)	(38)	(42)
Others	(15)	(14)	(19)	(22)	(25)	(29)	(33)	(38)	(44)
Imports, c.i.f.	-406	-367	-363	-404	-446	-452	-476	-502	-530
Cash	(-156)	(-73)	(-115)	(-105)	(-80)	(-88)	(-95)	(-102)	(-110)
Grants-in-kind	(-151)	(-180)	(-156)	(-215)	(-227)	(-223)	(-231)	(-239)	(-247)
Loans-in-kind	(-99)	(-114)	(-92)	(-83)	(-140)	(-141)	(-150)	(-161)	(-173)
Services (net)	-47	-55	-70	-51	-44	-36	-31	-26	-22
Interest payments	(-44)	(-49)	(-60)	(-48)	(-44)	(-37)	(-32)	(-27)	(-23)
Other	(-3)	(-6)	(-9)	(-3)	(-)	(1)	(1)	(1)	(1)
Transfers	246	225	232	282	255	253	262	271	281
Private	(72)	(20)	(37)	(27)	(28)	(30)	(31)	(32)	(33)
Official	(174)	(205)	(195)	(255)	(227)	(223)	(231)	(239)	(247)
Capital account	6	54	15	62	77	79	90	87	102
Official (net)	46	73	48	62	77	79	90	87	102
Inflows	(106)	(122)	(108)	(123)	(140)	(141)	(150)	(161)	(173)
Outflows	(-60)	(-49)	(-60)	(-61)	(-62)	(-61)	(-60)	(-73)	(-71)
Private	-40	-19	-33	--	--	--	--	--	--
Overall balance	-139	-50	-87	5	-27	-9	7	9	27
Financing	139	50	87	-5	27	9	-7	-9	-27
Central Bank	13	28	15	-50	-40	-38	-30	-12	-10
Reserves	(9)	(-2)	(16)	(-8)	(-6)	(-4)	(-5)	(-3)	(-3)
IMF (net)	(-3)	(32)	(-7)	(-5)	(-12)	(-35)	(-25)	(-9)	(-6)
Other	(7)	(-2)	(6)	(-38)	(-22)	(-)	(-)	(-)	(-)
Commercial bank	29	-32	-8	--	--	--	--	--	--
Arrears	71	-98	80	-66	-36	-21	--	--	--
Debt relief	26	152	--	...	...	...	...	...	...
Current debt service	(-)	(43)	(-)	(...)	(...)	(...)	(...)	(...)	(...)
Arrears	(26)	(109)	(-)	(...)	(...)	(...)	(...)	(...)	(...)
Financing gap	--	--	--	111	103	68	23	3	-17
Memorandum items:									
Current account excluding official transfers in US \$ millions	-319	-309	-297	-313	-331	-311	-314	-317	-322
GDP in US\$ at 1973 ppp rate in US\$ million	1,037	1,133	1,435	1,546	1,666	1,795	1,934	2,083	2,245
Gross reserves (in weeks of total imports)	--	1	3	4	4	4	5	5	5
Current account/GDP (in percent)									
Including official transfers	-14.0	-9.2	-7.1	-3.8	-6.3	-4.9	-4.3	-3.7	-3.3
Excluding official transfers	-30.8	-27.3	-20.7	-20.2	-19.9	-17.3	-16.2	-15.2	-14.3

Sources: Data provided by the Somali authorities; and Fund staff estimates.

1/ Financing gaps shown are before rescheduling.



Somalia's external accounts are of such magnitudes that sustainability will only be achieved over several years and will require, not only the implementation of strong domestic financial policies, but also of continued donor support.

Somalia has not been able to recover from the loss of a major export market for livestock in 1983. Despite efforts to find new outlets for livestock, the success of Somalia's efforts to expand its exports has been hampered by the balance of payments difficulties that some of its major customers have encountered. Thus, in the Gulf area, it has become more difficult for Somalia to expand sheep and goat exports, while the price received for these exports has tended to decline. In addition, some of the new markets found by Somalia have been unable to absorb the quantity of cattle which they have contracted because of payment difficulties. The recent depreciation in the exchange rate is providing Somalia with an added advantage in retaining a strong position in its traditional markets, but its ability to expand exports will also depend on developments in the importing countries. Somalia has entered into new contracts for cattle exports, while receiving assurances that the unfulfilled portion of the 1986 contracts will be taken up during 1987. On this basis, livestock exports are expected to increase by about 11 percent in 1987 in U.S. dollar terms. Growth could be higher if economic conditions improve in the Gulf area and if the new exchange arrangements reduce the extent of under-invoicing. Banana and other minor exports showed considerable strength in 1986. The former expanded by over 30 percent, while the latter rose by over one-third. On the basis of the banana replantings which took place in 1985-86, continued strong growth is expected from this sector and exports are projected to rise by about one-third in 1987. Other minor exports will be aided by exchange rate incentives and other supply-side measures being implemented by the authorities, but the effects of these factors will be felt over the medium term and this growth is projected to fall to about 16 percent in 1987. Overall, exports in 1987 are projected to rise by about 16 percent in U.S. dollar terms.

Somalia's adjustment policies require the continued containment of import demand. Imports fell by 10 percent in 1985 and by a further 1 percent in 1986. For 1987 they are expected to almost recover the 1984 level in U.S. dollar terms, largely as a result of imports related to the public investment program, which are fully financed by donor assistance. Locally financed imports are expected to fall slightly, largely as a result of the demand-management policy in effect and the depreciation of the exchange rate.

Apart from being large, Somalia's debt service includes a very high proportion of nonreschedulable debts. About US\$84.5 million (or 54 percent) of 1987 debt service is due to multilateral organizations. They also account for about US\$48.7 million (or 34 percent) of outstanding arrears as of December 1986. The rest of the debt service obligations are to bilateral governments and institutions, and, in principle, are

subject to rescheduling. The authorities have indicated their intention to seek a rescheduling of these amounts and have already approached the Paris Club for a possible date. Given the large amount of nonrescheduable debt, Somalia can obtain only a limited amount of balance of payments relief from a rescheduling. Nevertheless, the rescheduling of current debt service and arrears from bilateral sources is an important supporting element of the program. Arab countries and institutions are important creditors and arrangements for debt relief have not been negotiated. None of the Arab creditors participated in the 1985 Paris Club. Arrears to the Fund were liquidated in May, and the authorities will be paying two-thirds of outstanding arrears to multilateral organizations in the course of 1987, with the remainder to be liquidated in 1988. On the basis of the additional assistance obtained in 1987 and a projected rescheduling of Somalia's bilateral debts, the balance of payments gap for 1987 is closed. However, in 1988, in addition to a rescheduling of maturities due to bilateral institutions, an additional assistance of about US\$20 million in cash form will be required. The financing gap is reduced substantially in subsequent years, but Somalia will continue to require debt relief in conjunction with assistance in the form of cash.

The balance of payments for 1986-87 is heavily influenced by a one time emergency assistance program from Italy, which will provide over these two years about Lit 400 billion (SDR 235 million) to Somalia. These grant resources will provide for an important expansion in development projects and imports. A large portion of the disbursements will take place in 1987. Despite this unusually large concentration, the current account balance, when measured at the constant 1973 purchasing power parity rate, will record a decline both before and after grants in terms of GDP.

Because of Somalia's debt service difficulties, the program includes an embargo on the contracting or guaranteeing of any nonconcessional loans with a maturity of 1-12 years or any short-term credit, other than import credits and credits required in the rescheduling of external debt, or bridge loans that may be necessary to repay outstanding arrears to multilateral organizations. Over the last few years, almost all of Somalia's capital inflows have been in the form of grants and concessional loans.

## (2) Fiscal policy

Fiscal developments in 1985 and 1986 resulted in higher deficits than targeted, both excluding and including grants. In 1985, the deficit (commitment basis) reached over 13 percent of GDP (excluding grants) or about 4 percentage points of GDP higher than envisaged. Grants were slightly below target and the deficit including grants reached 6.2 percent of GDP compared to 2.0 percent in the program. This outturn resulted from a shortfall in revenue performance of over 2 percent of GDP, due to a shortfall in imports, delays in adjusting the import valuation factor, and administrative difficulties related to the

establishment of a new Ministry of Revenue, in combination with a 1.4 percent of GDP overrun on expenditures. The expenditure overrun, however, was focused on ordinary expenditures (2 percent of GDP) and domestically financed development outlays; foreign financed development expenditure was substantially less than expected because of delays in launching new projects. Despite this, net foreign financing was significantly above the level envisaged as a result of non project assistance. Nevertheless, domestic bank financing reached So. Sh. 1.1 billion, rather than the So. Sh. 0.1 billion programmed.

For 1986, the deficit overrun was considerably less than in 1985, with the deficit (excluding grants), reaching 14.2 percent of GDP rather than the expected 13.8 percent. Including grants the deficit rose moderately to 6.6 percent of GDP. However, in contrast to expectations, there was a large accumulation of government arrears on debt service (2 percent of GDP), and consequently the cash financing requirement was lower than programmed and essentially met from net foreign borrowing. In reaching this outturn (and in contrast with 1985) revenue performance exceeded expectations by over 1 percent of GDP due to improved administration. However, this improvement was only sufficient to offset a shortfall in grants. Expenditure was again substantially higher than envisaged because of much higher than expected ordinary and domestically financed development outlays. Foreign financed investment fell below target. The 1987 program aims at improving resource mobilization, controlling the level of ordinary expenditures, and strictly budgeting counterpart funds, with the view of limiting the Government's utilization. These policies aim at reducing the overall budgetary deficit and reducing net domestic indebtedness. The Government has recently increased tariffs on a large number of consumer goods aimed at raising an additional So. Sh. 100 million in the second half of 1987. In addition, a contract has been negotiated with a foreign firm to provide regular lists of minimum sales prices on imports to help the customs service reduce underinvoicing of imports. These measures are expected to raise revenue by about 0.4 percent of GDP in 1987. Meanwhile, the Ministry of Revenue will be undertaking a review of the tax system aimed at increasing the ratio of revenue to GDP further. On the basis of these studies, measures will be introduced in 1988 and 1989 to increase revenues by about 2 percentage points of GDP over the two-year period.

For the first time, a ceiling has been fixed on the utilization of the local currency counterpart of foreign commodity aid. A certain amount will be utilized for budgetary expenditures, with the rest to be deposited with the banking system and subject to a 100 percent reserve requirement.

In 1987 the expenditure control role of the Accountant General has been increased to limit unauthorized expenditures. Representatives of the Accountant General will be located in all spending ministries, and they will be required to review expenditure vouchers before they are sent to the Central Bank for payment. In addition, a quarterly review

of expenditure levels will be undertaken. A ceiling on ordinary expenditures has been established and a monthly reporting system put into place. Over the last few years, the Government has virtually eliminated transfers to public enterprises. The 1987 budget supports the continuation of this policy.

In conjunction with the World Bank, the Government has reviewed the public investment program (PIP) for the period 1987-89. The agreed planning level for the program is US\$1,025 million. On the assumption of a slippage factor of 30 percent, PIP expenditure is estimated at US\$720 million over the three years. The program was presented to and endorsed by the Consultative Group meeting held in Paris in April 1987. The program is fully financed mainly by grants. In selecting the projects for the PIP, priority was given to projects that rehabilitate existing facilities, remove infrastructural bottlenecks, or yield a high return in the short term. Expenditures in the productive sectors account for 86 percent of the PIP. Transportation and communications will absorb about 29 percent of PIP expenditures, with the agricultural sector absorbing an additional 29 percent. The Bardhere dam project alone will be responsible for 9 percent of investments. Most of the projects are ongoing, thereby permitting an improvement in the implementation level of the current three-year PIP. In addition, the Ministry of Planning has been strengthened through the assistance of a UNDP planning group. The National Monitoring and Evaluation Facility has been expanded and upgraded to the level of a Department, with a central role in monitoring the public investment program. Efforts are also being made to improve the statistical data base for planning, and there will be more frequent reviews of the development program to assure that it is on track. The authorities are more confident that the slippage factor can be reduced and the targeted level of investment realized. However, shortfalls in development expenditure will not lead to budgetary savings because the program is almost totally foreign financed. The Government intends to keep a tight employment policy and find ways of reducing the budgeted positions in line with the reform of the civil service.

On the basis of the above policy framework, domestic revenues are expected to reach So. Sh. 12.7 billion (7.5 percent of GDP) in 1987 compared with So. Sh. 9.5 billion in 1986 (6.9 percent of GDP) (Table 7). Grants, including counterpart funds to commodity assistance, are projected at So. Sh. 27.9 billion, providing total revenues and grants of So. Sh. 40.6 billion, compared with So. Sh. 19.9 billion in 1986. Ordinary expenditures are targeted at So. Sh. 17.9 billion compared with So. Sh. 16.2 billion in 1986. In terms of GDP, ordinary expenditures are projected to fall by about 1.2 percentage points to 10.6 percent of GDP. The Government's investment outlays are set at So. Sh. 32.8 billion, compared with So. Sh. 12.8 billion in 1986. A substantial part of the increase reflects the exchange rate depreciation and the temporary emergency Italian assistance program. Excluding these elements, the program remains at about the same size as the 1986 program. On a commitment basis, the overall deficit, including grants,

Table 7. Somalia: Summary of Government Operations, 1984-90 <sup>1/</sup>

	1984 Est.	1985 Prog. <sup>2/</sup>	1985 Est.	1986 Prog. <sup>3/</sup>	1986 Rev. est.	1987 Proj.	1988 Proj.	1989 Proj.	1990 Proj.
(In billions of Somali shillings)									
Revenue and grants	6.0	14.5	11.8	19.7	19.9	40.6	45.2	52.9	60.3
Revenue	(4.0)	(7.8)	(5.2)	(8.3)	(9.5)	(12.7)	(17.8)	(22.7)	(26.5)
Grants <sup>4/</sup>	(2.0)	(6.7)	(6.6)	(11.4)	(10.4)	(27.9)	(27.4)	(30.2)	(33.8)
Total expenditure	11.3	16.5	17.9	28.4	29.0	50.7	57.2	63.8	70.1
Ordinary	(8.2)	(7.9)	(9.9)	(10.9)	(16.2)	(17.9)	(22.1)	(25.8)	(27.7)
Investment	(3.1)	(8.6)	(8.0)	(17.5)	(12.8)	(32.8)	(35.1)	(38.0)	(42.4)
Domestic development budget	0.6	1.2	1.4	2.1	3.1	3.4	3.8	4.1	4.4
Public investment program	2.5	7.4	6.6	15.4	9.7	29.4	31.3	33.9	38.0
Overall deficit, commitment basis	-5.3	-2.0	-6.1	-8.7	-9.1	-10.1	-12.0	-10.9	-9.8
Change in domestic counterpart of external arrears	1.8	-1.8	-1.4	-0.8	2.8	-1.9	-1.4	-1.5	--
Other adjustments to cash basis	--	--	0.3	--	--	--	--	--	--
Overall deficit, cash basis									
Including grants	-3.5	-3.8	-7.2	-9.5	-6.3	-12.0	-13.4	-12.4	-9.8
Excluding grants	-5.5	-10.5	-13.8	-20.9	-16.7	-39.9	-40.8	-42.6	(-43.6)
Financing									
Foreign (net)	0.9	3.7	5.0	6.8	6.5	4.5	7.0	8.2	10.1
Drawings	(...)	(...)	(...)	(...)	(7.7)	(11.9)	(15.5)	(17.4)	(19.8)
Amortization	(...)	(...)	(...)	(...)	(-1.2)	(-7.4)	(-8.5)	(-9.2)	(-9.7)
Domestic	2.6	0.1	1.1	-0.3	-0.2	-0.5	-0.5	--	-0.3
Debt relief	--	--	1.1	--	--	--	--	--	--
Financing gap	--	--	--	3.0	--	8.0	6.9	4.2	--
(In percent of GDP)									
Revenue and grants	9.2	14.9	12.3	13.6	14.5	23.9	21.9	22.1	22.4
Revenue	(6.2)	(7.7)	(5.4)	(5.7)	(6.9)	(7.5)	(8.6)	(9.5)	(9.9)
Grants	(3.0)	(7.2)	(6.9)	(7.9)	(7.6)	(16.4)	(13.3)	(12.6)	(12.5)
Total expenditure	17.3	16.9	18.5	19.5	21.1	29.9	27.6	26.7	26.1
Ordinary	(12.5)	(8.1)	(10.3)	(7.5)	(11.8)	(10.6)	(10.7)	(10.8)	(10.3)
Investment	(4.8)	(8.8)	(8.2)	(12.0)	(9.3)	(19.3)	(16.9)	(15.9)	(15.8)
Domestic development budget	0.9	0.3	1.4	1.5	2.3	2.0	1.8	1.7	1.6
Overall deficit, commitment basis									
Including grants	-8.1	-2.0	-6.2	-5.9	-6.6	-6.0	-5.7	-4.6	-3.7
Excluding grants	-11.2	-9.2	-13.1	-13.8	-14.2	-22.4	-19.0	-17.2	-16.2
Change in domestic counterpart of external arrears	2.8	-1.9	-1.5	-0.6	2.0	-1.1	-0.8	-0.6	--
Overall deficit, cash basis									
Including grants	-5.3	-3.9	-7.4	-6.5	-4.6	-7.1	-6.5	-5.2	-3.7
Excluding grants	-8.3	-11.1	-14.3	-14.4	-12.2	-23.5	-19.8	-17.8	-16.2
Financing									
Foreign (net)	1.4	3.7	5.2	4.7	4.7	2.7	3.4	3.4	3.8
Domestic	3.9	0.1	1.1	-0.2	-0.1	-0.3	-0.2	--	-0.1
Debt relief	--	--	1.1	--	--	--	--	--	--
Financing gap	--	--	--	2.0	--	4.7	3.3	1.8	--
Memorandum									
GDP at current market prices (billions of Somali shillings)	64.99	97.76	96.42	145.41	137.46	169.92	206.81	238.89	269.57

Sources: Data provided by the Somali authorities; and staff estimates.

<sup>1/</sup> Based on an exchange rate of So. Sh. 26 per U.S. dollar for 1984, So. Sh. 39.5 per U.S. dollar for 1985, So. Sh. 71.9 per U.S. dollar for 1986, So. Sh. 130 per U.S. dollar for 1987, So. Sh. 146 per U.S. dollar for 1988, So. Sh. 161 per U.S. dollar for 1989, and So. Sh. 172 per U.S. dollar for 1990.

<sup>2/</sup> SM/86/225; based on average official exchange rate of So. Sh. 40 = US\$1 assumed in the program.

<sup>3/</sup> SM/86/225; based on average official exchange rate of So. Sh. 72.5 = US\$1 assumed in the program.

<sup>4/</sup> Includes cash grants, grants in kind, project grants, and commodity import program.

is targeted to fall to 6.0 percent of GDP, compared with 6.6 percent in 1986. Excluding grants, the deficit will increase to 22.4 percent of GDP from 14.2 percent, as a result of the large Italian emergency assistance grant. The overall deficit is expected to be financed by foreign resources, including debt relief, and to provide for an improvement in the Government's net position with the banking system equivalent to 0.3 percent of GDP in 1987. In the medium term, a reduction in both measurements of the deficit is expected.

### (3) Monetary policy

Monetary policy will contribute to a reduction in external and internal imbalances by aiding in the control of aggregate demand through a reduced growth of broad money and by promoting a shift of credit resources to the private sector. Key to the monetary policy objectives is a reduction of net credit to the Government by about 8 percent and progress in limiting credit growth to public enterprises. Interest rates on domestic currency time and savings deposits will be increased by 2 percentage points with the exception of the maximum deposit rate, which, at 24 percent is already positive when compared with the targeted inflation rate (as indicated in Table 2). Interest rates will be kept under review and will be increased further, if the inflation rate does not ameliorate as projected.

On the basis of the financial policies in place, net domestic credit is targeted to grow by 7.3 percent of the initial broad money during 1987 (Table 8). This is consistent with an expansion of broad money by about 13 percent, excluding foreign currency deposits, which have a 100 percent reserve requirement and therefore do not finance domestic credit, and counterpart funds which will have the same requirement. The credit ceilings on net domestic credit and net credit to the Government included in Table 9 are consistent with these annual projections, taking into account seasonal factors. This table also summarizes the other performance criteria of the program. Given the reduction in net credit to the Government, credit for the rest of the economy can grow by 18 percent in 1987, which is considered ample to bring about the necessary growth in income. Credit to public enterprises will be largely limited to enterprises in the process of restructuring.

#### b. Structural adjustment measures

The exchange and financial measures previously described will have an important impact in furthering the stabilization of the economy and also in improving the allocation of resources. However, these measures are not sufficient to promote the more rapid expansion of the economy by themselves, and additional supply-oriented measures will be needed to improve the growth prospects of the economy and to lay the groundwork for the development in the longer term. In the policy framework paper, the Government details certain important structural adjustment and supply-side measures which are aimed at removing bottlenecks which

Table 8. Somalia: Monetary Survey, 1982-87

	1982	1983	1984	1985	1986	1987 Proj.
(In millions of Somali shillings)						
Net foreign assets <u>1/</u>	347.4	-1,061.6	-2,585.6	-2,212.6	-9,680.1	-10,653.6
Net domestic credit	5,023.8	5,260.8	9,616.2	11,516.9	13,904.3	14,852.0
Government (net)	2,100.0	1,805.0	4,378.1	5,421.8	6,079.1	5,579.1
Others	2,923.8	3,455.8	5,238.1	6,095.1	7,825.2	9,272.9
Public enterprises	1,300.0	1,163.0	1,511.2	2,071.2	3,730.4	...
Private	1,623.8	2,292.8	3,726.9	4,023.9	4,094.8	...
Monetary liabilities	4,994.6	5,348.1	6,677.8	11,606.9	16,051.7	18,640.2
Local currency	4,994.6	5,348.1	6,547.2	9,520.8	13,043.6	14,752.3
Counterpart funds	...	...	75.4	211.7	1,031.3	515.3
Foreign currency deposits	...	...	55.2	1,874.4	1,976.8	3,372.6
Other items (net)	376.6	-1,418.9	352.8	-2,302.6	-11,827.5	-14,441.8
Valuation adjustment	-514.1	-1,551.6	-1,447.0	-6,124.1	-19,104.6	-32,593.8
Medium- and long-term loans <u>1/</u>	988.2	1,318.8	2,059.8	3,655.1	8,077.8	13,781.3
Other liabilities (net)	-97.5	-916.1	-260.0	166.4	-800.7	4,370.7
(Percentage change in relation to broad money)						
Net domestic credit	10.9	4.7	81.4	29.0	25.1	7.3
Government (net)	-3.4	-5.9	48.1	15.9	6.9	-3.8
Others	14.4	10.7	33.3	13.1	18.2	11.1
Public enterprises	-9.7	-2.7	6.5	8.6	17.4	...
Private	24.0	13.4	26.8	4.5	0.7	...
(Annual percentage change)						
Net domestic credit	10.5	4.7	82.8	19.8	20.7	6.8
Government (net)	-6.7	-14.0	142.6	23.8	12.1	-8.2
Others	27.3	18.2	51.6	16.4	28.4	18.5
Public enterprises	-24.5	-10.5	29.9	37.1	80.1	...
Private	182.6	41.2	62.5	8.0	1.8	...
Monetary liabilities	14.4	7.1	24.9	73.8	38.3	16.1
Local currency	14.4	7.1	22.4	45.4	37.0	13.1
Counterpart funds	...	...	...	180.8	387.2	-50.0
Foreign currency deposits	...	...	...	3,295.7	5.5	70.6

Sources: Central Bank of Somalia; and staff estimates.

1/ Includes valuation adjustments.

Table 9. Somalia: Quantitative and Nonquantitative Performance Criteria

A. Quantitative Performance Criteria, 1985-87

	1985 Dec.	April	1986 July	Dec. 1/	March 1/	1987 June	Sept.	Dec.
(In millions of Somali shillings, end of period)								
Net domestic credit 2/								
Ceiling	10,150.0	12,200.0	12,409.0	12,438.0	13,987.0	14,360.0	14,560.0	14,852.0
Actual	11,516.9	12,132.1	12,395.1	13,904.3	...	...	...	...
Net credit to Government 3/								
Ceiling	4,448.0	5,800.0	5,945.0	5,360.8	5,831.0	5,800.0	5,630.0	5,580.0
Actual	5,421.8	6,184.7	5,941.1	6,079.1	...	...	...	...

(In millions of U.S. dollars)

New external borrowing contracted or guaranteed by the Government								
a. 1-12 year maturity								
Ceiling	--	--	--	--	--	--	--	--
Actual	--	--	--	--	...	...	...	...
b. Short-term borrowing 4/								
Ceiling	...	24.0	24.0	24.0	--	--	--	--
Actual	...	21.3	7.7	--	...	...	...	...

B. Nonquantitative Performance Criteria, 1987

Petroleum prices

Domestic petroleum and fuel prices will be fixed at import parity as measured by the prevailing auction rate. This performance criteria will be tested prior to each drawing.

Interest rates

Increase interest rates by 2 percentage points, on all but the longest maturity deposit.

Exchange Losses Related to the Petroleum Accounting Rate

Petroleum imports will be transacted for a temporary period not to exceed December 31, 1987 at a rate of So. Sh. 105 per U.S. dollar, and any exchange losses that the Central Bank may incur in these transactions will be reimbursed by the petroleum importing agency.

Reviews 5/

A review of the exchange system, the financing of the balance of payments gap for 1988, budgetary policy and performance criteria for the remaining period of the arrangement, will take place before the end of December, 1987.

With the assistance of the Fund's resident representative, a quarterly review of government ordinary expenditure will be conducted to ensure that it does not exceed the programmed level.

Payments Restrictions

The Government of Somalia will continue to maintain a liberal exchange and trade system and will not introduce any new or intensify existing restrictions, and will remain current on all its obligations with the Fund.

Sources: Central Bank of Somalia; and staff estimates.

1/ Indicative ceilings.

2/ Net domestic credit comprises credit to Government, public enterprises, and the rest of the private sector, less government deposits with the banking system.

3/ Net credit to Government comprises the banking system's claims on the Government, less Government deposits (excluding local currency counterpart funds deposits at the Commercial Bank) and excludes the escrow account for the counterpart funds.

4/ In 1986, limited to short-term borrowing, with the exception of normal trade credit, which may be necessary to repay the Fund. The ceilings for 1987 are zero, excluding normal trade credit, such arrangements as may emerge from debt rescheduling, and bridge loans that may be necessary to repay outstanding arrears to multilateral organizations.

5/ In addition there will be a consultation with the Managing Director on the auction system, budgetary policy, petroleum pricing, and interest rate policy prior to the end of July 1987.



hinder increased production. A detailed description of these measures is included in Table 10.

Over the last few years, many measures have already been implemented to facilitate productive activity. Important among these are the removal of most pricing and import restrictions and the reduction of monopolies in the agricultural sector. Pricing policies have been generally liberalized, and agricultural prices are market determined. The Agricultural Development Corporation (ADC) has become a price stabilization board. The role of the National Trading Agency has been reduced to deal only with food aid imports, and it no longer competes with private sector activities. The Government aims to limit further its activities in the directly productive sectors and to encourage the private sector to absorb some public enterprises.

(1) Agriculture and livestock

Agriculture is considered Somalia's key development sector. Although only about 13 percent of Somalia's total land area is considered arable, only a small percentage of this land is actually cultivated. The Government's medium-term strategy emphasizes grain production and greater food self-sufficiency. A growth rate of over 5 percent per annum can be sustained in the agricultural sector, provided that investments are made in irrigation rehabilitation, in the development of new irrigation facilities, and in improved water management. The current PIP strongly emphasizes agriculture, with over 29 percent of planned investments in this sector, with livestock accounting for 7 percent, crops 14 percent, and fishery and forestry 8 percent. Of the planned investment in crop agriculture, almost two-thirds is oriented for irrigation infrastructure, especially for the rehabilitation of existing systems. The Government is in the process of preparing an action plan to increase the irrigation efficiency of Somalia by 30 percent in the medium term. The projects which will support this target have been included in the present PIP. The short-term objectives of this program include increasing the water storage capacity of the Shebelli irrigation area and refurbishing the physical works and water control mechanisms.

The Government is committed to further reduce the role of government monopolies in the agricultural sector. This will provide an added area of action for the private sector. The Government will provide the World Bank, by June 30, 1987, a program of action in the marketing and pricing of hides and skins. A study will be initiated with the same objective with regard to frankincense and myrrh. The Government proposes to encourage agricultural production by the timely distribution of agricultural inputs. The ADC will begin bulk importation of agricultural inputs in 1987. Traders and farmers will be encouraged to stock the inputs for resale and a credit mechanism will be implemented in 1987 to facilitate the stocking.

Table 10. Somalia: Summary and Time Frame for Macroeconomic and Structural Adjustment Policies, 1987-89

	Objectives and targets	Strategies and measures	Timing of measures	Commitments for implementation in 1987	Commitments in 1987 for implementation in 1988/89
<b>1. External and Trade Sector Policies</b>					
a. Exchange rate.	Promote exports and efficient resource allocation.	Unify the rates.	Early 1987.	Implement enhanced foreign exchange auction for imports and services. Export proceeds and private transfers, which are not utilized by receiver, will be surrendered at auction rate. All official and private transactions with the temporary exception of oil imports to be at the auction rate.	Abolish the temporary petroleum rate by December 1987.
		Maintain a flexible exchange rate system.	1987 onwards.		
	b. External borrowing and debt management.	No new government or government-guaranteed external borrowing at nonconcessional terms in the 1-12 years maturity range. Limits on short-term borrowing.	Continue in 1987, 1988, 1989.	No new government or government-guaranteed external borrowing at nonconcessional terms in the 1-12 years maturity range. Limits on short-term borrowing.	Continuing.
		Remain current on nonreschedulable obligations and secure debt rescheduling agreements with Paris Club (and other creditors).	1987, 1988, 1989.	Seek Paris Club rescheduling in May, 1987, on the basis of expected balance of payments support provide payment of 1987 nonreschedulable debt service.	Continue making nonreschedulable debt service payments on time.  Seek Paris Club rescheduling in 1988 and 1989.
		Reduce non-reschedulable arrears and gradually increase international reserves.	1987, 1988, 1989.	Nonreschedulable arrears (excluding IMF and AMF) be reduced by one third in 1987, and international reserves targeted to increase by US\$8 million.	Nonreschedulable arrears (excluding IMF and AMF) to be reduced by one half in 1988, and eliminated in 1989. Reserves to be increased by US\$7 million, and US\$5 million in 1988 and 1989, respectively.
c. Tariff structure.	Rationalize tariff structure to promote efficiency objectives.	Undertake measures to reduce wide dispersion in nominal and effective rates of protection.	1988 onwards.	Tariffs to be reviewed with the aim of raising at least So. Sh. 100 million in the second half of 1987.	With the help of a foreign donor review tariff structure and customs procedures in 1987 and implementation reforms beginning in 1988.

Table 10. Somalia: Summary and Time Frame for Macroeconomic and Structural Adjustment Policies, 1987-89 (continued)

	Objectives and targets	Strategies and measures	Timing of measures	Commitments for implementation in 1987	Commitments in 1987 for implementation in 1988/89
<b>2. Policies to Promote Production</b>					
a. Agricultural pricing and marketing.	Promote production and exports.	Maintain liberal agricultural pricing and marketing.		Review agricultural support prices on a yearly basis and continue with a free market for grains, with ADC serving as a price support agency only.	
		*Complete study of marketing and pricing of hides and skins and frankincense and myrrh, and formulate appropriate incentive policies in light of study recommendations.	Continue in 1987, 1988, 1989.	Study of marketing and pricing of hides and skins was completed in February 1987.	Study the present problems of frankincense and myrrh.
		Take measures to improve incentives for production and exports of frankincense and myrrh.	1987.	Research is taking place in the domestication of frankincense so that it can be produced on farms.	Additional policy proposals to promote production and exports of frankincense and myrrh will be implemented in 1988.
		Encourage private sector agro-processing.	1987, 1988.		
		Remove obstacles to domestic movement of outputs and inputs.	1987.	ADC will begin bulk importation of agricultural inputs. Traders and farmers will be encouraged to stock the inputs for resale. A credit mechanism will be implemented in 1987 to facilitate the stocking.	Continuing.
		*Liberalize marketing and exports of hides and skins.	1988.	The authorities will present a plan of action to the World Bank, to improve sector efficiency by June 30, 1987.	Continuing.
		*Improve livestock quality and marketing, including through fostering greater role for private sector in supply of inputs and services.	Continue in 1987, 1988, 1989.	In addition to rangeland improvements, projects are being implemented to provide fodder supply on stock routes, and for the expansion of veterinary services.	Continuing.

Table 10. Somalia: Summary and Time Frame for Macroeconomic and Structural Adjustment Policies, 1987-89 (continued)

	Objectives and targets	Strategies and measures	Timing of measures	Commitments for implementation in 1987	Commitments in 1987 for implementation in 1988/89
		Encourage additional private sector involvement in the production and export of fruits and vegetables.	1987.	There will be an expansion of extension services for citrus in 1987. Expansion of production in the Shebelli irrigation area will be promoted.	Efforts to link farmers with buyers abroad will be promoted. The expansion of Somali Airlines will take into account the need for cargo space for fruits and vegetables to the Gulf countries, as well as lower freight rates.
		Take measures to improve incentives and extension services to expand and diversify crop and exports.	Over the program period.	Extension services of the Ministry of Agriculture will be expanded, especially in the irrigated areas.	Continuing.
b. Petroleum pricing and distribution.	Improve efficiency of resource allocation.	*Fully decontrol petroleum prices and allow independent private agents to import and distribute in competitive environment.	1987.	Petroleum products will continue to be priced at import parity with reference to the prevailing auction rate, but distribution will remain the monopoly of one cooperative. Private companies may import petroleum products for their own uses as at present.	Continuing.
c. Management of food aid.	Maintain incentives for domestic producers and encourage food import substitution.	*Implement actions agreed under IDA credit for ASAP concerning minimum and ceiling prices for foodgrains and sales of food aid.	1987, 1988.	Commitments under IDA, ASAP credit to be met.	Continuing.
		Control food aid inflow; marketing and pricing to be consistent with domestic food production objectives.	1986 onwards.	Expand the early warning system, established in 1986, to prevent drought-related food shortages. This will assist in establishing food aid requirements.	Continuing.
d. Land tenure and rights.	Improve conditions for private investment in agriculture and recovery of land changes.	*Study land tenure arrangement.	1987.	Coordinate timing of imports with donor.	
		Rationalize land rights and tenure.	1988.	A revised Land Tenure Law to be prepared in 1987.	Law revision expected to be approved in 1988.
e. Water management.	Improve irrigation efficiency.	*Study the problem.	1987.		
		Implement substantial cost recovery and water control measures.	1988.	An action plan aimed at increasing irrigation efficiency by 30 percent in the medium term has begun to be implemented. Projects that will support this objective are included in the present PIP.	Continue with irrigation improvements. Expand User Association to improve allocation. Increase water charges to encourage higher value crops.
				Immediate objectives are the following:	

Table 10. Somalia: Summary and Time Frame for Macroeconomic and Structural Adjustment Policies, 1987-89 (continued)

Objectives and targets	Strategies and measures	Timing of measures	Commitments for implementation in 1987	Commitments in 1987 for implementation in 1988/89
			<p>1. Increase the water storage capacity of Shebelli irrigation area.</p> <p>2. Refurbish the physical works and rehabilitate water control mechanisms.</p>	
<b>3. Public Sector Management</b>				
a. Investment selection.	Raise quality and productivity of public investment.	Include in PIP only projects with highest economic returns, emphasize (i) rehabilitation and utilization of productive capacity; and (ii) investments to facilitate production of tradeable commodities in private sector.	Begin in 1987 for large projects and continue in 1988, 1989.	Agree on the size and composition of the PIP at the Consultative Group meeting in April, 1987, following World Bank review of 1987-89 PIP.
b. Investment size; coordination of investment and expenditure plans.	Improve macro-economic management.	Contain size within implementation capacity, present and prospective recurrent cost financing ability, external resource availability and within targets for budget expenditure and domestic credit.	Begin in 1986 and continue in 1987, 1988, 1989.	<p>Stay within guidelines for the core PIP as agreed. Annual tranches to be implemented in 1988 and 1989 to be reviewed with Bank and Fund before the start of each year.</p> <p>Improve budgeting of recurrent costs.</p> <p>Establish monitoring group to review implementation of PIP on a quarterly base.</p>
c. Public enterprises.	Improve efficiency or resource allocation and use.	<p>(i) Undertaking feasibility studies for enterprises to be rehabilitated, and formulate time-specific action plan for rationalization of the PE sector. This will provide for, inter alia,</p> <p>(ii) Phasing out enterprises proved to face serious financial and/or economic problems.</p>	1987-1989.	<p>At the time of the forthcoming industrial sector mission, agree with the World Bank on the number and time frame of studies to be conducted in 1987, which are aimed at establishing the feasibility of enterprises by either rehabilitating or closing them down.</p> <p>Implement study recommendations on enterprises for which studies are complete, and continue with studies of other enterprises.</p>

Table 10. Somalia: Summary and Time Frame for Macroeconomic and Structural Adjustment Policies, 1987-89 (continued)

Objectives and targets		Strategies and measures	Timing of measures	Commitments for implementation in 1987	Commitments in 1987 for implementation in 1988/89
		(iii) Review the legal and institutional framework with a view to improving this framework, clarifying PR objectives and the respective roles of the public and private sectors, establishing satisfactory performance incentive and monitoring structures, and providing more autonomy to enterprise managers.	1987.		
		Undertake economic and financial studies of Somaltex, cigarette and match factory, Edible Oil Mill, Somalmeat, and aluminium utensils factory.	1987.	Priorities to be decided with World Bank.	
		Urea plant and refinery.	1988.		
		Set up unit in Ministry of Industry and Commerce to supervise public enterprises.	1987.	A unit will be set up to monitor public enterprises.	
d. Civil service reform.	Improve productivity of public administration.	Establish a system of posts grading and performance evaluation, reduce size of civil service, and selectively raise salaries to provide incentives to productivity; finance salary increases through raising revenues and cutting non-developmental ordinary expenditures for general services.	1987.	Salaries in 1987 were increased for the first time since 1981, by about 30 percent. Discussions with interested donors will continue with the aim of establishing a program for implementing a formal reform.	Framework for civil service reform will be negotiated with foreign donors.
<b>4. Financial and monetary policies</b>					
a. Financing plan.	Budgetary discipline and stabilisation; improve financial discipline and macro-economic management.	Improve public sector accounting practices and make budget more transparent; prepare realistic financing plan for 1987-89 with estimates of all domestic and external resources, investment and recurrent expenditure, including debt service.	1987 onwards.	Only expenditures with vouchers duly authorized by the Accountant General's office will be paid by the Central Bank. Counterpart funds will be budgeted and a ceiling established on their utilization on a yearly basis.	Continuing.

Table 10. Somalia: Summary and Time Frame for Macroeconomic and Structural Adjustment Policies, 1987-89 (concluded)

	Objectives and targets	Strategies and measures	Timing of measures	Commitments for implementation in 1987	Commitments in 1987 for implementation in 1988/89
b. Fiscal measures.	Public sector resource mobilization; eliminate current budget deficit.	Increase revenues by converting specific excise taxes to ad valorem basis; evaluate import duties using free market exchange rate and reduce import tax exemption.		Initiate review of the tax system with the aim of rationalizing the structure and increasing revenues in relation to GDP.  Raise revenues by 70 percent in 1987, 85 percent in 1988, and 90 percent in 1989.	Implement tax reform.
		Centralize at the Central Bank any surplus counterpart funds over a ceiling of So. Sh. 10.5 billion.	1987, 1988, 1989.	All counterpart funds generated by donor assistance programs, in excess of So. Sh. 10.5 billion are to be subject to a 100 percent reserve requirement to be maintained in an escrow account.	Continuing.
		Impose ceilings on transfers to public enterprises and on current expenditures of ministries; limit payments of benefits-in-kind.	1987, 1988, 1989.	Ceilings on current expenditure by ministries have been established for 1987.	Continuing.
	Improve funding of recurrent expenditures.	Restructure current expenditures to raise share of social and economic services.		A special allocation for maintenance is included in the 1987 budget.	Continuing.
				Raise the share of social and economic services to 20 percent in 1988, 30 percent in 1989.	
c. Credit and interest rate.	Mobilize domestic savings and improve credit allocation.	Observe ceilings on growth rates of total domestic credit, net credit to the Government and credit to the public enterprises.	1987, 1988, 1989.	Domestic credit growth to be restricted to 13.1 percent in 1987, and net credit to the Government will decline by 8.2 percent. Credit to public enterprises to be limited mainly to those that are being rehabilitated.	Credit program to be established each year.
		Issue the decree allowing other commercial banks to operate.	1987.	Decree establishing Cooperative Bank issued on ..., allows the creation of other banks.	
		Raise interest rates to ensure positive interest rates in real terms; maintain a flexible interest rate policy.	1987 onwards.	Interest rates on all but the largest maturity deposits will be raised by 2 percentage points, with most time deposit rates and the main lending rate reaching real positive levels in comparison to the targeted inflation.	To be reviewed yearly.

It appears that the rangelands in Somalia are rapidly approaching the limit to their ability to sustain additional animals. If the livestock sector is to contribute significantly to the growth of income in the medium term, improved rangeland management and other measures to raise productivity will be required. Studies will begin in 1987 to confirm the carrying capacity of Somalia's rangelands. In addition, in order to improve the quality of the livestock on its way to market, projects are being implemented to provide fodder on stock routes and for the expansion of veterinary services. These projects include the setting-up of quarantine stations, which would allow Somalia to certify the health of the animals being exported, and hopefully open up markets in the Gulf which have been closed to Somalia since 1983.

An expansion of the production of fruits and vegetables can have a significant impact on the growth of the agricultural sector and possibly exports. It will also increase the value of production in many of the irrigated areas. The authorities plan for an expansion of extension services for citrus, in 1987, and will promote their growth in the Shebelli irrigated area. Later on, efforts will be made to link farmers with foreign buyers in order to promote exports.

The authorities are committed to maintaining the ADC's functions as a price stabilization board that will guarantee minimum prices. Market forces will be allowed to set actual farmgate prices. In the past, the arrival of food aid has been counterproductive in maintaining the incentives to domestic producers because it has arrived mainly at harvest time, thereby depressing domestic prices. A management committee will be assuring that negotiations on commodity food aid are held in such a way that it would allow their arrival at a more propitious date. In addition, the early warning system established in 1986 to prevent drought-related food shortages is being expanded. This will assist in more accurately establishing food aid requirements.

The insecurity of present land tenure rights has been a handicap to increased private sector agricultural investment. The Government is presently studying the problem and will be preparing a revised land tenure law in 1987 for presentation to Parliament in 1988.

## (2) Industry and public enterprise sectors

The Government intends to promote private sector activity in the industrial sector, while, at the same time, improving the efficiency of the public enterprises through privatizing, restructuring and closing unprofitable ones. The opportunities for the private sector have already been expanded by a reduction in official monopolies, an increase in the availability of bank credit, the freeing of domestic prices, the removal of import and exchange controls, and the strengthening of the auction system. A new foreign investment act with incentives to attract foreign private investment was passed early in 1987, while a new department for the promotion of private investment has been established in the Ministry of Planning with technical assistance from a foreign



donor. Despite these efforts, a major improvement in industrial growth over the medium term will only be possible through the restructuring of public enterprises because they dominate Somalia's industrial sector. In the short term the restructuring of enterprises is likely to keep the growth of industry at a low level. Industrial output has fallen since the late 1970s, and this has been reflected in a low capacity utilization of public enterprises. In order to improve the efficiency of public enterprises, the Government will undertake feasibility studies of enterprises and formulate a specific action plan for their rationalization. By July 1987, the Government will have agreed with the World Bank on a time frame for this work and on the list of public enterprises which will be studied in the first year. The Government has already closed down some enterprises, while others which are inefficient have ceased physical operations, although the enterprises have not been disbanded. With the help of the World Bank, the Government expects to strengthen its drive for reforming the public enterprises. To facilitate the Government's immediate control over public enterprises, a unit is being set up in the Ministry of Industry to monitor developments in public enterprises. In addition, an effort is being made to limit domestic credit only to public enterprises which are in the process of restructuring.

## 2. Benchmarks

For the purpose of monitoring progress in the implementation of the first annual arrangement under the structural adjustment facility, the following benchmarks will be observed: (i) limit net domestic credit to So. Sh. 14.85 billion on December 31, 1987 and So. Sh. 15.47 billion on June 30, 1988; (ii) continue to price petroleum products at import parity level; (iii) implement an enhanced foreign exchange auction; (iv) apply for a Paris Club rescheduling; (v) increase the role of the Accountant General in the expenditure process by June 1987; (vi) provide a plan of action for ADC, including provisions for the bulk importation of agricultural inputs and for the resale by private traders and farmers in the rural sector by December 1987; (vii) initiate a review of the tax system by September 1987; (viii) prepare a timeframe for the study and review of public enterprises with the World Bank by March 1988; (ix) implement an expansion of extension services for citrus by December 1987; (x) initiate discussions with major donors for the financing of the civil service reform; and (xi) review agricultural support prices in early 1988. On the basis of the expected assistance and other balance of payments developments, the Central Bank's net foreign assets are targeted to improve by about US\$50 million in 1987 and by a further US\$40 million in 1988. However, given the seasonal factors involved in the first semester of 1988 net foreign assets are projected to fall by about US\$4 million from the beginning year level by end-June 1988.

### 3. Social impact of adjustment

The adjustment process so far has had a very positive impact on the income of the rural sector. The trade reforms have enhanced the incomes of the population engaged in livestock and crop production, while the liberalization of markets and the reduction of government regulations have reversed previously discriminatory policies which subsidized urban consumption at the expense of rural producers. The greater use of market allocation mechanisms has served to reduce economic rents accruing to a small class of the relatively well-off. Consequently, the urban sector has seen its privileges reduced through the adjustment effort, especially so, as wages have lagged considerably behind the increases in the cost of living. In addition, the transitional costs of the adjustment process including the laying off of redundant government and parastatal workers will fall largely upon lower income urban groups. All income groups are affected by the removal of price controls and by the increased relative prices of imported consumer goods, but the urban sectors are likely to be affected the most. The fiscal measures will have a mixed social impact. The targeted increase in revenues will effect mainly the upper income groups, while the expected shift in the composition of recurrent expenditures in favor of more social and economic services would have a positive social impact in both the short and the long run. Over the longer run, even those groups adversely affected in the short run are expected to benefit from the adjustment program, since it will enhance the longer-term prospects for growth and equity. In the transitional period, special provisions will have to be made and special training and placement programs will have to be formulated to enable the displaced civil service and parastatal workers to find employment elsewhere. This is an inherent aspect of the civil service reform. The Government will seek donor assistance to help plan and administer these programs.

### III. Staff Appraisal

In 1985 and 1986 Somalia renewed its efforts to adjust and stabilize the economy, with mixed results. The magnitude of the initial imbalances and difficulties in developing and maintaining the necessary political consensus to persevere with the adjustment policies, which delayed the introduction of agreed upon policies, were detrimental to the success of the program. Despite difficulties in fully complying with the statistical objectives of the previous stand-by arrangement and temporary departures in the policy thrust of the program, significant progress has been made in adjusting the economy, especially in strengthening the initial progress made in reducing controls and liberalizing the economy. These actions represented a major reversal of the Government's economic philosophy, and were politically difficult to introduce and to maintain because they did not have universal support. In this setting, the Government was courageous in persevering with the reform movement. Progress in this regard was made possible by continued generous donor support for Somalia's stabilization efforts. Without

this support, the success achieved to date would not have been possible.

Somalia continues to face difficult economic circumstances and its future is clouded, not only by large financial imbalances, but also by severe development problems, which arise from Somalia's low income level and poor natural endowment. The financial imbalances are of large magnitudes, and progress in their resolution will be slow and difficult, and will require additional sacrifices. To attain its present objectives, the Government will require generous donor assistance over a period of many years, including debt relief and additional cash assistance.

The authorities' program for 1987-89 is a balance between the need to further stabilize the economy by reducing financial imbalances, and to set the groundwork that will encourage long-term development and growth, while protecting the level of real per capita consumption.

The program does not have much margin of maneuverability. Delays in the implementation of agreed upon policies or in the release of foreign assistance will have negative implications for the attainment of the program's targets. Because of this constraint, the program includes a strengthened reporting system and reviews, including those with the Managing Director.

In view of the wide-ranging structural commitments in the program which are relying on the completion of studies, an unusual degree of responsibility will fall upon the Government and on the creditors helping the Government complete the studies to reach agreement on the required policies quickly and for their prompt implementation. The staff will follow the evaluation of the studies closely.

The reform of the public enterprises is a key element in allowing for a more rapid expansion of the economy. The forthcoming discussions between the Government and the World Bank, which will establish the agenda for the work in this sector, should provide the necessary framework, and the authorities are encouraged, with the help of the World Bank, to move quickly to implement the necessary studies and to take the reform measures as quickly as possible.

Substantial progress has been made in liberalizing the economy, but there are still some restrictive practices which inhibit the maximum development of Somalia's export potential. Through the policies agreed in the current program, most of these restrictive practices will be terminated.

An improvement in the domestic mobilization of resources is an important objective of the program. The present program provides a balance between the need to increase savings and to contain the level of aggregate expenditure. Financial imbalances will only be reduced in line with the authorities' success in reducing the overall budgetary deficit, through improvements in domestic resource mobilization and in

the structure of government expenditure. The authorities' objective of increasing revenues in relation to GDP is an important element in this regard. The constraint on credit and monetary expansion specified in the program will aid in reducing inflationary pressures, while the expected net government repayments to the banking system will provide the necessary financing for increased private sector activity. The expanded auction system, the increased credit facilities for the private sector, and the reduction of government intervention in the productive sectors will provide an enhanced environment for the private sector to improve its level of economic activity.

Somalia's balance of payments will remain critical for a number of years, reflecting a small coverage of exports over imports and the very high debt service ratio projected for a number of years. However, the strengthening of production incentives and an improvement of the control on aggregate demand will promote further external adjustment, which, together with continued donor support, will allow the projected financing gap to be reduced over a number of years. The enhanced auction system recently launched has substantially narrowed the difference between exchange rates and will play an important role in promoting the reduction of imbalances. By the end of 1987, the exchange system will be fully unified with the removal of the special accounting rate for petroleum.

The balance of payments relies heavily on foreign assistance. Foreign aid finances a substantial proportion of external payments. The problems encountered in the past in preparing an accurate cash flow for this assistance clearly point to the need for the Government and its major donors to better coordinate the flow of this assistance. The flow of orderly payments is also hampered by an inadequate level of gross foreign assets and by delays in reaching agreements with major donors on the modalities for debt relief.

Not all official bilateral creditors have found avenues to grant Somalia debt relief. Only a small proportion of Somalia's creditors participated in the 1985 Paris Club meeting. There is an urgent need for bilateral donors to find ways to grant Somalia debt relief during the proposed program period. The regularization of Somalia's debt service is one of the main objectives of the current program, but it will require the imaginative and concerted participation of all creditors. The successful completion of debt reschedulings, or other arrangements which grant debt relief, is likely to release additional resources for Somalia's development effort, and this would be highly welcome in assuring the success of the current development effort. The present foreign exchange availabilities are not sufficient to guarantee a minimum level of imports and to clear all outstanding arrears to multilateral agencies within the current calendar year. However, such arrears are expected to be liquidated by the end of 1988. In the event that foreign assistance is greater than previously projected, a more rapid schedule of payments will be effected.

Somalia's exchange system has been progressively liberalized and simplified in recent years, with the elimination of the separate commercial bank rate for foreign exchange, the availability of foreign exchange through the recognized free market, and the reduction of external payments arrears. Somalia at present maintains an exchange restriction evidenced by the remaining commercial arrears, and multiple currency practices arising from the operation of the official, free, and auction exchange markets. A multiple currency practice is also expected to arise temporarily from the introduction and maintenance of a special exchange rate for petroleum imports until December 1987. In view of the authorities' intentions to further liberalize the system, merging the multiple exchange markets into the existing auction market in June 1987 and by eliminating arrears and supporting policies, the staff recommends that the Executive Board grant approval for the maintenance by Somalia of the exchange restriction and multiple currency practices, until December 31, 1987, or the next Article IV consultation with Somalia, whichever is the earlier.

Somalia's medium-term prospects remain fragile and will rely heavily not only on the timely implementation of the policies included in the program, but also on the continuing reviews of developments to ascertain that the thrust of the program is maintained.

Foreign exchange availabilities in Somalia are highly dependent on foreign assistance. Exports and remittances in 1987 are projected to cover only 35 percent of imports, while Somalia faces a high debt service burden. In addition, export earnings are concentrated in the second semester of the calendar year. Somalia has virtually no foreign reserves. Despite the authorities' willingness to earmark a proportion of their export earnings to meet Somalia's obligations to the Fund, which in 1987 are equivalent to 35 percent of export earnings, the high seasonality of exports and delays in the receipt of foreign aid in cash form are likely to result in Somalia continuing to incur overdue obligations to the Fund from time to time. The authorities give a high priority to discharging Somalia's obligations to the Fund and in 1986 75 percent of all debt service payments made by Somalia were to the Fund.

The staff urges the authorities to put into place the necessary means to maintain their payments to the Fund current.

Mogadishu  
June 5, 1987

Dear Mr. Camdessus:

We would like to take this opportunity to thank the Fund for the assistance it has granted to Somalia in the past, which has been important in supporting the Government's adjustment efforts, and in generating needed donor support. In view of our continuing balance of payments difficulties, we would like to continue with the close relations that exist between the Fund and Somalia.

The Government of Somalia has prepared an economic and financial policy framework that contains the objectives of government policy for the three-year period 1987-89. The programs and the policy initiatives have been discussed with the staffs of the World Bank and the Fund. Under this policy framework, the Government's plans for 1987 are detailed in the attached memorandum on economic and financial policies.

The Government of Somalia requests that the program contained in this document be supported by Fund resources under a structural adjustment facility loan and a stand-by arrangement. The details of policy measures contained in this document are for calendar 1987. A program for the remaining period of these arrangements will be discussed with the Fund at an appropriate time.

The Government would like to request that the stand-by arrangement cover a period of 20 months, or through January 1989, to allow the program to serve as a basis for a rescheduling of Somalia's debt service obligations of 1987-88.

The Government of Somalia intends to consult with the Managing Director on the auction system, budgetary policy, petroleum pricing, and the interest rate policy, prior to the end of July 1987. In addition, it intends to review and reach understandings with the Fund prior to end-December 1987 on the exchange system, the financing of the balance of payments gap for 1988, budgetary policies, and the performance criteria for the remaining period of the stand-by arrangement.

During the program period, the Government of Somalia will continue to maintain a liberal exchange and trade system and will not introduce any new or intensify existing restrictions, and will remain current on all its financial obligations with the Fund.

Somalia will provide the Fund with such information as the Fund requests in connection with its progress in implementing the policies and achieving the objectives of the program.

The Government of Somalia believes that the policies outlined in the memorandum on economic and financial policies are adequate to achieve the objectives established for 1987, but will take any further measures that may become appropriate for this purpose. The Government will consult with the Fund on the adoption of any measures that may be appropriate at the initiative of the Government, or whenever the Managing Director requests consultation because he considers that consultation under the program is desirable.

Sincerely yours,

Dr. Mohamed Sheik Osman  
Minister of Finance

Dr. Omar Ahmed Omar  
Governor,  
Central Bank of Somalia

Mr. Michael Camdessus  
Managing Director  
International Monetary Fund  
Washington D.C., 20431

Memorandum on Economic and Financial Policies

1. In recent years the Government of Somalia has viewed its economic and financial policy in terms of a medium-term framework. This approach is being strengthened by the further integration of economic policies under the guidelines of a macroeconomic and structural framework that has been discussed with the World Bank and the Fund. On this basis the Government has strengthened economic policy in order to reduce the external and internal imbalances in the economy, while laying the groundwork for sustained economic development. The program detailed below represents a continuing effort by the Government to address Somalia's difficult economic situation. However, without continued strong donor support the program will have only limited success.

2. As indicated in the policy framework paper, the basic objectives of the program for 1987-89 are: (a) to achieve an average growth rate of real GDP of about 4 percent per annum; (b) to reduce the growth of the cost of living from the 31 percent recorded in 1986 to about 22 percent in 1987, 15 percent in 1988, and about 8-10 percent in 1989; (c) to reduce further the external current account deficit, excluding official grants, (d) to strengthen Somalia's development effort, while at the same time reducing the overall deficit of government operations to GDP. The program aims at maintaining the level of real per capita private sector consumption levels, while encouraging an improvement in private sector savings and an increase in private sector investment. In the public sector, government revenues are expected to increase their ratio to GDP in order to permit the reduction in the deficit of government operations. The development program will be strengthened by an improved and more efficient allocation of resources, including a "core" investment program that will emphasize the rehabilitation of existing assets, and increased capacity utilization in commodity production and exports. These government objectives will require a better allocation of current expenditures, which will increase the availability of maintenance expenditures and provide resources for a reform of the civil service. In investment, a higher rate of implementation of the development program is expected. Improved production incentives will also be implemented in order to allow the private sector to play a more meaningful role in the development of the country. In pursuing these objectives, the Government will implement a credit policy conducive to an expansion of broad money that is consistent with reducing inflationary pressures, but which because of government net repayments to the banking system, will provide ample resources for private sector activity. At the same time, the regularization of Somalia's debt service will be furthered through reschedulings and the payment of arrears to multilateral organizations. A more detailed description of the objectives of the three-year program is found in the policy framework paper and its matrix. Below are the details of the first annual program.



a. Sectoral policies

3. The limitations to the more extensive use of the rangelands will mean that there will be reduced prospects for the growth of livestock, and that the expansion of the economy will only be possible through diversification. Grain production will be emphasized. The investment program will give a high priority to the rehabilitation of irrigation facilities and new investments.

4. The fishing subsector has considerable growth potential. The existing fishing operations are of small size and the Government intends to improve these operations and to foster a more critical and commercial approach in the fishing parastatal, with priority given to artisanal private sector undertakings. In 1987 a review of the sector's operations will be conducted and the development program strengthened.

5. Manufacturing output will be promoted through the reform of the public enterprises, including the rehabilitation of viable enterprises and the closing of inefficient ones, and improved incentives to the private sector.

6. A study of the marketing and pricing of hides and skins has recently been completed by UNIDO. The authorities are reviewing the recommendations and will provide the World Bank, by June 30, 1987, a plan of action that will make the sector more efficient and expand exports.

7. The investment program to be implemented in the next three years also includes projects that will improve livestock quality in order to increase export earnings. In addition to rangeland improvements, these projects include the provision of fodder supply on stock routes and the expansion of veterinary services.

b. External policies

8. Since September 1986 a twice a month foreign exchange auction has been held for imports largely from resources arising from the Agricultural Sector Adjustment Program (ASAP) financed by IDA. Beginning in February 1987, assistance from the U.S. and Italy has begun to be channeled through the auction, which during its several months of operations has attracted considerable participation and has functioned well. The Government has temporarily enhanced the existing auction market, which will simplify the existing exchange arrangements, and greatly unify the exchange markets. All export proceeds will be surrendered to the Central Bank at the auction rate. The auction rate, defined as the weighted average rate of successful bids, will be published regularly by the Central Bank, and will apply to all transactions except as specified below. Together with foreign commodity import assistance, up to 50 percent of export proceeds will be auctioned for imports, with the remaining export proceeds reserved for debt service and official transactions. The auctions will aim to provide

US\$100 million in 1987 distributed as uniformly as is consistent with seasonal factors. The Government of Somalia and the Fund will consult from time to time on the operations of the auction at the request of either party. Inward transfers by individuals and private and public enterprises will continue to be received freely through external accounts at the Commercial Bank. All transfers of other entities shall accrue to external accounts at the Central Bank and shall be transacted at the auction rate. Holders of external accounts at the Commercial Bank may continue to use them for their own purposes through the Commercial Bank. Transfers between external accounts will no longer be permitted, but holders may sell the proceeds to the banking system at the service auction rate. The Commercial Bank may be allocated foreign exchange at the service auction at the weighted average rate of successful bids for resale between auctions. Petroleum imports (about half of which are being provided through aid agreements in 1987) will be transacted for a temporary period not to exceed December 31, 1987, at a rate of So. Sh. 105 per U.S. dollar. Domestic petroleum and fuel prices will be fixed according to the stipulations of the International Development Association (IDA) ASAP credit and the Treasury will receive any exchange gains that may arise after the Central Bank has been reimbursed for any exchange losses that it may incur in these transactions.

9. Holders of export promoting accounts and import accounts may continue to use the balance in their accounts for imports, but not to add to their balance as from ....., 1987.

10. Somalia has made considerable progress in recent years in moving towards a liberal trade and exchange system and will continue to maintain a liberal system. The minimum export surrender value for livestock will be reviewed periodically to ascertain that they reflect current market conditions.

c. Fiscal policy

11. In 1986 administrative improvements were largely responsible for the more than 80 percent increase in revenues, which allowed the ratio of revenues to GDP to reach 6.9 percent, compared to 5.4 percent in 1985. A further increase to 7.5 percent is expected in this ratio in 1987. In order to bring about this increase, Government will be implementing revenue measures that will generate 0.4 percent of GDP in the three-quarters that remain in the fiscal year. The measures detailed in Attachment 1 will be implemented for this purpose. On the basis of these measures, total revenues are now projected to reach So. Sh. 12.70 billion (7.5 percent of GDP) in 1987. Grants are projected to reach So. Sh. 27.95 billion (16.4 percent of GDP), of which about So. Sh. 5.46 billion are for budget support and So. Sh. 24.49 billion for projects. However the revenue and grants are likely to be larger, and a mid-year review of the budget will be undertaken in July together with the Fund. If at that time the revenue performance is better than presently estimated, a reduction in the Government's net

external and domestic indebtedness will be sought. Conversely, additional measures will be adopted if the review indicates the need in order to maintain the overall deficit target.

12. In the last few years investment outlays have been growing substantially, increasing their ratio to GDP to about 9 percent per year in 1985-86. Maintenance expenditures have not grown as rapidly to the detriment of the capacity utilization of government assets. The 1987 budget includes a special allocation for maintenance. In 1987 Somalia has suffered several armed incursions from a neighboring country, which have been repulsed, but which have increased defence requirements. These higher expenditures have come at a time when military aid to Somalia has been reduced drastically.

13. These factors, together with a general wage increase (the first since 1982 and averaging 30 percent), and the impact of the exchange rate adjustment, will account for an increase in ordinary expenditures in 1987, despite economies which have been made in other categories of outlays. Ordinary expenditures are now estimated at So. Sh. 17.95 billion (10.6 percent of GDP). A system of monthly reports will be instituted, and a review of ordinary expenditure will be held every quarter, with the help of the Fund's Resident Representative.

14. A three-year Public Investment Program (PIP) has been reviewed by the World Bank. The 1987 budget incorporates the first tranche of this program, including the projects being financed by emergency assistance from Italy (6.4 percent of GDP). Investment expenditures are projected to reach 19.3 percent of GDP, compared to an estimate of 9 percent for 1986. All of these expenditures are being financed by foreign donors, largely through grants or concessional financing. Most expenditures will be on on-going projects, with priority being given to projects that rehabilitate existing facilities. About 86 percent of the projects are in the productive sectors. Transport, communication, and agriculture each will account for about 29 percent.

15. The overall budgetary deficit (including grants) will decline to 6.0 percent of GDP in 1987, compared to 6.6 percent in 1986. Excluding grants the ratio will rise from 14.2 percent of GDP to 22.4 percent, largely because of the large Italian emergency grant. However, the deficit will allow for a small reduction in net domestic indebtedness, as prospective foreign financing, including the estimated debt relief, will more than finance the expected deficit.

16. Further improvements are to be implemented in the budgetary process during 1987. Only expenditures that have a duly authorized voucher that has been passed through the office of the Accountant General will be paid by the Central Bank. The counterpart funds from foreign assistance programs have become an important financing item for the budget. These are expected to finance 20.7 percent of total expenditures in 1987, compared to 29.3 percent in 1986. At the present time some of these resources are deposited in the Commercial Bank prior to the utilization for government expenditure, allowing the Commercial Bank to finance

credit operations in the interim. Funds received in excess of the budgeted amount will be deposited in the banking system and will be subject to a 100 percent reserve requirement, which will be kept in an escrow account.

17. A review of the tax system will be initiated in 1987 aimed at improving the efficiency of revenue collection and at maintaining an increasing ratio to GDP. Assistance for this exercise has already been arranged with some foreign donors. On the basis of this review additional measures will be implemented beginning in 1988, with the aim of gradually increasing the revenue performance and reducing the overall deficit.

18. During the year discussions for the formulation of the basis for civil service reform will continue, together with foreign donors from whom indications of support have been received, with the aim of establishing a program of action.

d. Monetary policy

19. Monetary policy in 1987 will aim at limiting the credit expansion to constrain the growth of aggregate demand, at increasing the level of gross foreign assets, and at providing for interest rates that promote a more efficient allocation of resources and encourage financial savings. For calendar 1987 growth of net domestic credit from the banking system will be limited to 6.8 percent, which is consistent with a 13.1 percent growth in local currency deposits. In order to attain this objective net credit of the banking system, which totaled So. Sh. 13.90 billion on December 31, 1986, will not exceed So. Sh. 14.36 billion on June 30, 1987, So. Sh. 14.56 billion on September 30, 1987, and So. Sh. 14.85 billion on December 31, 1987. Within this total net credit to the central government will fall by 8.2 percent in calendar 1987. To attain this objective net credit to the Government, which was So. Sh. 6.08 billion on December 31, 1986, will not exceed So. Sh. 5.80 billion on June 30, 1987, So. Sh. 5.63 billion on September 30, 1987, and So. Sh. 5.58 billion on December 31, 1987. The contraction of credit to the Government will allow for a more rapid expansion of credit to the private sector and public enterprises. Credit to the latter will be mainly available to those organizations that are in the process of being rehabilitated. In 1987 gross reserves of the Central Bank will be targeted to increase by US\$8 million. The attainment of this target will be influenced by the implementation of the program's policies and by the amount of additional foreign assistance attained in cash form. The balance of payments financing gap presented at the Consultative Group meeting contains an allocation for this purpose.

20. Under the thrust of the budgetary and credit policies described above there should be a significant lowering of inflationary pressures in the course of 1987. Already price increases have moderated considerably since October 1986, and the increase in the cost of living is expected to decelerate to 22 percent by the end of 1987, compared to 31 percent in 1986. At this level interest rates for some time deposits

would be positive in real terms. However, to better align the structure of interest rates, the deposit savings rates will be increased by 2 percentage points by April 15, 1987.

21. The establishment of a Cooperative Bank has been approved by the Government, through a decree issued on .... and the Government is encouraging the opening of other banks. The above decree contains the necessary amendments to the law that would allow establishment of other banks.

e. Public enterprises

22. To improve the allocation of domestic resources, major improvements in the management of public enterprises are required. For a number of years, the Government has pressed forward with this objective and several enterprises have been closed, while others have been rehabilitated, some under foreign management. Clearly the pace of reform has been slow, in comparison to the requirements. However, the Government has been severely handicapped by a shortage of trained personnel to conduct the necessary feasibility studies, a lack of resources with which to promote the rehabilitation of the enterprises, and a private sector which does not have the management or financial resources to take over many of the enterprises. With the help of the World Bank, the Government expects to make substantial progress in this area in the next three years. This program of assistance will commence with the arrival of an industrial mission from the World Bank in the near future. The Government will agree with the World Bank on a timeframe and on the number of enterprises that will be reviewed.

f. External financing gap

23. Continued balance of payments difficulties, including important delays in foreign assistance, have resulted in Somalia's inability to meet its external debt obligations on schedule. At the end of 1986, arrears on debt payments amounted to US\$143.1 million, of which US\$48.6 million were to multilateral organizations. Somalia will be asking major donors and creditors for assistance in regularizing debt service obligations through debt relief and some assistance in cash form. In this regard, a Consultative Group meeting was held in early April and a meeting of the Paris Club will be requested for early June. Contacts are also continuing with other donors, who have not traditionally participated in the Paris Club, for the negotiation of debt relief. However, without the assistance which is being requested, it will be virtually impossible for Somalia to meet its external debt obligations. Institutional, marketing, and other measures are limiting export growth to about 13 percent per annum in the next three years, despite the structural measures being implemented, unless a traditional market for cattle, which has been closed since 1983, is re-opened. Moreover, a further contraction in imports to release resources for debt service would be counter-productive in maintaining an adequate pace of development and export growth. On the basis of the requested

assistance, which includes a necessary component in cash and petroleum products, Somalia expects clear its outstanding arrears by the end of 1988.

24. At the present time, a financing gaps in the balance of payments of US\$111 million and US\$103 million are projected for 1987 and 1988. Debt relief could fill an overwhelming part of the gaps, but without a minimum assistance in cash or petroleum products of US\$30-40 million in 1987 and 1988, the regularization of the debt payments and the needed increase in foreign assets in the Central Bank will not be attained.

25. Because of the current debt difficulties, the Government will not contract or guarantee any nonconcessional loan with a maturity of 1-12 years or any short-term credits other than import credits, with the exception of arrangements that may emerge from debt reschedulings or bridge loans that may be necessary to repay outstanding arrears to multilateral organizations.

g. Performance criteria and benchmarks

26. As indicated above, to monitor progress under the program, the following quantitative performance criteria will apply:

(1) quarterly ceilings on net credit of the banking system;

(2) quarterly ceilings on net credit to the Central Government;

(3) An embargo on the contraction or guarantee of nonconcessional loans with a maturity of 1-12 years and short-term credits other than trade credits and arrangements that may emerge from debt reschedulings or bridge loans that may be necessary to repay outstanding arrears to multilateral organizations;

(4) an embargo on the introduction or intensification of exchange restrictions;

(5) a review of the program prior to December 1987. In addition to consultations with the Managing Director no later than July 1987 and July 1988 on the policies set forth in the Economic and Financial Memorandum.

27. For the purpose of the first annual arrangement under the Structural Adjustment Facility (SAF) the following will serve as benchmarks for the timetable of specific policy actions under the SAF:

(1) limit net domestic credit to So. Sh. 14.85 billion on December 31, 1987 and So. Sh. 15.47 billion on June 30, 1988;

(2) implement an enhanced foreign exchange auction beginning May 1987;

- (2) apply for a Paris Club rescheduling;
- (4) review agricultural support prices in early 1988;
- (5) provide a plan of action for ADC, including provisions for bulk importation of agricultural inputs and for the resale by private traders and farmers in the rural sector by December 1987;
- (6) implement an expansion of extension services for citrus by December 1987;
- (7) continue to price petroleum products at import parity level;
- (8) prepare a timeframe for the study and review of public enterprises with the World Bank by September 1987;
- (9) increase the role of the Accountant General in the expenditure process by June 1987;
- (10) initiate a review of the tax system by September 1987;
- (11) initiate discussions with major donors for the financing of civil service reform.

On the basis of the expected assistance and other balance of payments developments, the Central Bank's net foreign assets are targeted to improve by about US\$50 million in 1987 and by a further US\$40 million in 1988. However, given the seasonal factors involved in the first semester of 1988 net foreign assets are projected to fall by about US\$4 million from the beginning year level by end-June 1988.

Proposed Revenue Measures - 1987

1. A contract is being negotiated with Compagnie General de Surveillance (CGS) through which the customs service will be provided with lists of minimum sales prices on a periodic basis for the most important import commodities. These lists will be used to reduce the extent of misreporting of imports for customs purposes.
2. Tariffs are being reviewed with the aim of raising at least an additional So. Sh. 100 million in the second half of 1987.



SOMALIA - Stand-by Arrangement

Attached hereto are a letter and annexed memorandum dated June \_\_\_\_ 1987 from the Minister of Finance and Governor of the Central Bank of Somalia requesting a stand-by arrangement and setting forth the policies and objectives that the authorities of Somalia intend to pursue for the period of this stand-by arrangement and understandings of Somalia with the Fund regarding reviews that will be made of progress in realizing the objectives of the program and of the policies and measures that the authorities of Somalia will pursue for the remaining period of this stand-by arrangement.

To support these objectives and policies, the International Monetary Fund grants this stand-by arrangement in accordance with the following provisions:

1. For the period from \_\_\_\_\_ until January \_\_\_\_, 1989, Somalia will have the right to make purchases from the Fund in an amount equivalent to SDR 33.15 million, subject to paragraphs 2, 3, 4, 5, and 6 below, without further review by the Fund.
2. (a) Purchases under this arrangement shall not, without the consent of the Fund, exceed the equivalent of SDR 5.53 million until August 1, 1987, SDR 11.06 million until November 1, 1987, SDR 16.39 million until February 15, 1988, SDR 22.12 million until April 15, 1988, SDR 27.65 million until November 1, 1988.
3. (a) None of the limits in (a) above shall apply to a purchase under this stand-by arrangement that would not increase the Fund's holdings of Somalia's currency in the credit tranches beyond 25 percent of quota or increase the Fund's holdings of that currency resulting from purchases of supplementary financing or borrowed resources beyond 12.5 percent of quota.
4. Purchases under this stand-by arrangement shall be made from ordinary and borrowed resources in the ratio of 1 to 2, provided that any modification by the Fund of the proportions of ordinary and borrowed resources shall apply to amounts that may be purchased after the date of modification.
5. Somalia will not make purchases under this stand-by arrangement that would increase the Fund's holdings of Somalia's currency in the credit tranches beyond 25 percent of quota, or increase the Fund's holdings of that currency resulting from purchases of supplementary financing or borrowed resources beyond 12.5 percent of quota;
  - (a) during any period in which the data at the end of the preceding period indicate that
    - (i) the limit on net domestic credit of the banking system described in paragraph 19 of the annexed memorandum, or

- (ii) the limit on net credit to the Government described in paragraph 19 of the annexed memorandum,
- (iii) the target of petroleum and fuel prices described in paragraph 8,

is not observed; or

(b) after December 31, 1987, if the adjustment to an import parity of the auction rate import price specified in paragraph 8 is not observed; or

(c) if Somalia fails to observe

- (i) the embargo on the contracting of new public and publicly guaranteed foreign indebtedness of a maturity not exceeding one year, other than import credits or bridge loans that may be necessary to repay arrears to multilateral organizations,
- (ii) the embargo on the Government's contracting or guaranteeing of external borrowing on nonconcessional terms in the 1-12 year maturity range,

described in paragraph 25 of the annexed memorandum; and

(d) after October 31, 1987, until the review contemplated in the fifth paragraph of the attached letter is completed and suitable performance criteria have been established, or after such performance criteria have been established while they are not being observed; or

(e) during the entire period of this stand-by arrangement, if Somalia

- (i) imposes new or intensifies existing restrictions on payments and transfers for current international transactions, or
- (ii) introduces new or modifies existing multiple currency practices, or
- (iii) concludes bilateral payments agreements that are inconsistent with Article VIII, or
- (iv) imposes or intensifies import restrictions for balance of payments reasons.

When Somalia is prevented from purchasing under this stand-by arrangement because of this paragraph 4, purchases will be resumed only after consultation has taken place between the Fund and Somalia and

understandings have been reached regarding the circumstances in which such purchases can be resumed.

5. Somalia will not make purchases under this arrangement during any period of the arrangement in which the member has an overdue financial obligation to the Fund or is failing to meet a repurchase expectation pursuant to the Guidelines on Corrective Action in respect of a noncomplying purchase.

6. Somalia's right to engage in the transactions covered by this stand-by arrangement can be suspended only with respect to requests received by the Fund after (a) a formal ineligibility, or (b) a decision of the Executive Board to suspend transactions, either generally or in order to consider a proposal made by an Executive Director or the Managing Director formally to suppress or to limit the eligibility of Somalia. When notice of a decision of formal ineligibility or of a decision to consider a proposal is given pursuant to this paragraph 6, purchases under this arrangement will be resumed only after consultation has taken place between the Fund and Somalia and understandings have been reached regarding the circumstances in which such purchases can be resumed.

7. Purchases under this stand-by arrangement shall be made in the currencies of other members selected in accordance with the policies and procedures of the Fund, and may be made in SDRs if, on the request of Somalia the Fund agrees to provide them at the time of the purchase.

8. The value date of a purchase under this stand-by arrangement involving borrowed resources will be determined in accordance with Rule G-4(b) of the Fund's Rules and Regulations. Somalia will consult with the Fund on the timing of purchases involving borrowed resources in accordance with Rule G-4(d).

9. Somalia shall pay a charge for this arrangement in accordance with the decisions of the Fund.

10. (a) Somalia shall repurchase the outstanding amount of its currency that results from a purchase under this stand-by arrangement in accordance with the provisions of the Articles of Agreement and decisions of the Fund, including those relating to repurchases as Somalia's balance of payments and reserve position improves.

(b) Any reductions in Somalia's currency held by the Fund shall reduce the amounts subject to repurchase under (a) above in accordance with the principles applied by the Fund for this purpose at the time of the reduction.

(c) The value date of a repurchase in respect of a purchase financed with borrowed resources under this stand-by arrangement will be normally either the 6th day or the 22nd day of the month, or the next business day if the selected day is not a business day, provided that

repurchase will be completed not later than seven years from the date of purchase.

11. During the period of the stand-by arrangement, Somalia shall remain in close consultation with the Fund. These consultations may include correspondence and visits of officials of the Fund to Somalia or of representatives of Somalia to the Fund. Somalia shall provide the Fund, through reports at intervals or dates requested by the Fund, with such information as the Fund requests in connection with the progress of Somalia in achieving the objectives and policies set forth in the attached letter and annexed memorandum.

12. In accordance with the letter, Somalia will consult with the Fund on the adoption of any measures that may be appropriate at the initiative of the Government or whenever the Managing Director requests consultation because any of the criteria in paragraph 4 above have not been observed or because he considers that consultation on the program is desirable. In addition, after the period of the arrangement and while Somalia has outstanding purchases in the upper credit tranches, the Government will consult with the Fund from time to time, at the initiative of the Government or at the request of the Managing Director, concerning Somalia's balance of payments policies.

Somalia: Schedule of Purchases during Period of  
Stand-by Arrangement, June 1987-January 1989

Amount	Scheduled availability	Conditions necessary for purchase <u>1/</u>
SDR 5.53 million	June , 1987	Board approval of program
SDR 5.53 million	After August 1, 1987	Compliance with quantitative performance criteria as of June 30, 1987 and completion of review with Managing Director
SDR 5.53 million	After November 1, 1987	Compliance with quantitative performance criteria as of September 30, 1987 and completion of program review
SDR 5.53 million	After February 15, 1988	Compliance with quantitative performance criteria as of December 31, 1987
SDR 5.53 million	After April 15, 1988	Compliance with quantitative performance criteria as of March 31, 1987
SDR 5.53 million	After November 1, 1988	Compliance with quantitative performance criteria as of September 30, 1988

1/ Other than generally applicable conditions under the arrangement and non-quantitative performance criteria (including the performance clause on the exchange and trade system).

Somalia: Three-year and First Annual Arrangements  
Under the Structural Adjustment Facility

In the letter with an annexed Memorandum on Economic and Financial Policies in Appendix I dated June 5, 1987, from the Minister of Finance and the Governor of the Central Bank of Somalia requesting from the Fund a three-year structural adjustment arrangement and the first annual arrangement thereunder, and setting forth

(i) the objectives and policies of the program to be supported by the three-year arrangement,

and

(ii) the objectives and policies of the program to be supported by the first annual arrangement.

To support these objectives and policies, the International Monetary Fund grants the requested arrangements in accordance with the following provisions and subject to the Regulations for the administration of the Structural Adjustment Facility:

1. For a period of three years from \_\_\_\_\_, 1987 Somalia will have the right to obtain three successive loans from the Fund under the Structural Adjustment Facility in a total amount equivalent to SDR 20.774 million.

2. The first loan, in an amount equivalent to SDR 8.84 million, is available for disbursement at the request of Somalia.

3. The second and third loans will be available upon approval by the Fund of the corresponding annual arrangements and will be disbursed at the request of Somalia. The amount of the second loan will be equivalent to SDR 5.967 million, and the amount of the third loan will be equivalent to SDR 5.967.

4. Before approving the second annual arrangement, the Fund will appraise the progress of Somalia in implementing the policies and reaching the objectives of the program supported by the first annual arrangement, taking into account primarily:

(a) the indicators described in paragraph 27 of the Memorandum of Economic and Financial Policies,

(b) imposition or intensification of restrictions on and payments transfers for current international transactions,

(c) introduction or modification of multiple currency practices,

(d) conclusion of bilateral payments agreements which are inconsistent with Article VIII,

(e) imposition or intensification of import restrictions for balance of payments reasons.

5. In accordance with the seventh paragraph of the letter, Somalia will provide the Fund with such information as the Fund requests in connection with the progress of Somalia in implementing the policies and reaching the objectives supported by the first annual arrangement.

6. In accordance with the eighth paragraph of the letter, Somalia will consult with the Managing Director on the adoption of any measures that may be appropriate at the initiative of the Government or whenever the Managing Director requests consultation because he considers that consultation on the program is desirable. These consultations may include correspondence and visits of officials of the Fund to Somalia or of representatives of Somalia to the Fund.

SOMALIA - Relations with the Fund  
(As of April 30, 1987)

I. Membership Status

- |                         |                 |
|-------------------------|-----------------|
| (a) Date of membership: | August 31, 1962 |
| (b) Status:             | Article XIV     |

A. Financial Relations

(Amounts in millions of SDRs, unless otherwise indicated)

II. General Department

- |  |                                  |
|--|----------------------------------|
| (a) Quota:                                   | 44.2                             |
| (b) Total Fund holdings of Somali shillings: | 162.94 (368.64 percent of quota) |
| (c) Fund credit:                             | 118.73 (268.63 percent of quota) |
| Of which: credit tranches                    | 16.94 (38.32 percent of quota)   |
| enlarged access                              | 69.19 (156.55 percent of quota)  |
| compensatory financing facility              | 32.60 (73.76 percent of quota)   |

III. Current Stand-By or Extended Arrangement and Special Facilities

(a) Latest stand-by arrangement:

- |   |      |
|---|------|
| (i) Duration from February 22, 1985 to September 30, 1986 |      |
| (ii) Amount   | 20.1 |
| (iii) Utilization   | 20.1 |
| (iv) Undrawn balance                                      | --   |

(b) Previous stand-by arrangements during the last 10 years:

- |   |      |
|---|------|
| (i) Duration from July 15, 1982 to January 14, 1984 |      |
| (ii) Amount:  | 60.0 |
| (iii) Utilization:                                  | 60.0 |
| (iv) Undrawn balance:                               | --   |

- |  |      |
|--|------|
| (i) Duration from July 15, 1981 to July 14, 1982 |      |
| (ii) Amount:                                     | 43.1 |
| (iii) Utilization:                               | 43.1 |
| (iv) Undrawn balance:                            | --   |

- |  |  |
|--|--|
| (i) Duration from February 27, 1980 to |  |
|--|--|



SOMALIA - Relations with the Fund (continued)

	February 26, 1981	
(ii)	Amount:	11.5
(iii)	Utilization:	6.0
(iv)	Undrawn balance:	5.5

(c) Special facilities (current year and past two years):

(i) Compensatory financing facility  
(effective February 22, 1985)

Amount:	32.6
Utilization:	32.6

IV. SDR Department

(a)	Net cumulative allocations:	13.7
(b)	Holdings:	None

V. Administered Accounts

(a) Trust Fund loans

(i)	Disbursed:	10.69
(ii)	Outstanding:	8.57

(b)	SFF Subsidy Account	None
-----	---------------------	------

VI.	<u>Overdue Obligations to the Fund as at 5/7/87:</u> (millions of SDRs)	17.98
-----	--	-------

VII. Somalia has used Fund resources since 1964.

B. Nonfinancial Relations

VIII. Exchange Rate Arrangement:

On January 1, 1985 Somalia established a dual exchange rate system whereby the official rate applies to all official transactions and the surrendered portion of export receipts, and the market rate applies to all other transactions. The official exchange rate, which was set at So. Sh. 36 = US\$1 on January 1, 1985, was pegged to the SDR adjusted for relative price developments vis-à-vis the five countries included in the SDR basket. The daily exchange rate was to be maintained within margins of 7.5 percent around the fixed real-term relationship to the SDR with indicative bands of 2.25 percent. There was, moreover, to be an additional devaluation of So. Sh. 0.5 per U.S. dollar each month of the official rate. For the second half of 1985, agreement on the exchange regime for the official exchange rate was not reached, and the rate remained at So. Sh. 40.6083 = US\$1 from June 5 to November 1, 1985. On November 2, 1985, the official rate was devalued by So. Sh. 1.8917 per U.S. dollar bringing it in line with the earlier agreement

SOMALIA - Relations with the Fund (continued)

to devalue by So. Sh. 0.5 per U.S. dollar per month. On January 21, 1986 the official rate was devalued by So. Sh. 12 per U.S. dollar, and for the months of March-November, the rate was further devalued in accordance with decisions reached in November and January to devalue the rate by So. Sh. 4 on the first of each month. These monthly devaluations continued to November 1986, at which time the official rate was So. Sh. 90.5 = US\$1. This has been maintained through April 1987.

The posted rate at the commercial bank, which had been maintained at So. Sh 84.4 per U.S. dollar since April 1985, was unified with the official rate on October 1, 1986. Beginning on September 1, 1986, the Central Bank initiated bi-monthly foreign exchange auctions. The weighted average rate at the April 16, 1987 (Dutch) auction was So. Sh. 128.6 per U.S. dollar and the lowest successful bid was So. Sh. 127.0 per U.S. dollar. The free market rate during the first two weeks of April 1987 averaged So. Sh. 154 per U.S. dollar.

IX. Article IV Consultation, Stand-By Review, and Discussions  
of 1987 Program

Discussions for the 1986 Article IV consultation and final review of the 1985 stand-by arrangement were held in Mogadiscio on July 9-21, 1986. The staff report (SM/86/225 and Correction 1) and the review under the stand-by arrangement (SM/86/217) were discussed by the Executive Board on September 22, 1986. The decisions adopted were as follows:

1986 Consultation

Executive Board Decision - September 22, 1986

1. The Fund takes this decision relating to Somalia's exchange measures subject to Article VIII, Sections 2(a) and 3, and in concluding the 1986 Article XIV consultation with Somalia, in the light of the 1986 Article IV consultation with Somalia conducted under Decision No. 5392-(77/63) adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. Somalia maintains a restriction on the making of payments and transfers for current international transactions as evidenced by the accumulation of some commercial arrears, and multiple currency practices, subject to Fund approval under Article VIII, Sections 2(a) and 3, as described in SM/86/234. The Fund notes the intention of the Government of Somalia to eliminate the multiple currency practices, which were approved through December 31, 1986 (Executive Board Decision No. 8282-(86/81), adopted May 12, 1986), in the context of the adjustment program described in EBS/86/93. The Fund grants approval of the restriction evidenced by the accumulation of commercial arrears through December 31, 1987 or the next Article IV consultation with Somalia, whichever is earlier.

SOMALIA - Relations with the Fund (continued)

Review of Stand-by Arrangement

1. The Government of Somalia has consulted with the Fund in accordance with paragraph 4 of the stand-by arrangement for Somalia (EBS/81/1, 1/2/85) as amended, and paragraph 35 of the letter attached thereto as modified by paragraph 20 of the letter dated April 22, 1986, from the Minister of Finance and the Governor of the Central Bank of Somalia, concerning deviations in the observance of the performance criteria under paragraph 4 of the stand-by arrangement, and in order (a) to review progress made by Somalia in realizing the objectives of its program, (b) to reach understandings on the balance of payments gap, exchange rate and budgetary and petroleum pricing policies that the authorities will pursue during the period through September 30, 1986, and (c) to establish suitable performance criteria for the rest of the program.

2. The letter dated September 16, 1986, from the Minister of Finance and the Governor of the Central Bank of Somalia, setting forth policies and measures that the authorities will pursue, shall be annexed to the stand-by arrangement for Somalia and the letters of November 8, 1984, and April 22, 1986, shall be read as modified and supplemented by the letter dated September 16, 1986.

3. Somalia will not make purchases under the stand-by arrangement that will increase the Fund's holdings of Somalia's currency in the credit tranches beyond 25 percent of quota, or increase the Fund's holdings of that currency resulting from purchases of borrowed resources beyond 12.5 percent of quota, during any period in which the data at the end of the preceding period indicate that:

- (a) the limit on total domestic credit of the banking system described in paragraph 10 of the letter of September 16, 1986, or
- (b) the limit of net credit from the banking system to the Government described in paragraph 10 of the letter of September 16, 1986,

is not observed.

4. The Fund decides, pursuant to paragraph 4 of the stand-by arrangement, that the review contemplated in paragraph 35 of the letter of November 8, 1984, as modified by paragraph 20 of the letter of April 22, 1986, is completed and that no additional understandings are necessary; and that notwithstanding the nonobservance of the performance criteria on net credit to the Government for April 30, 1986, Somalia may resume to make purchases under the stand-by arrangement.

SOMALIA - Relations with the Fund (continued)

X. Technical Assistance:

- (a) FAD: From December 1983 to March 1986 an Advisor from the FAD assisted the Ministry of Finance as tax advisor.
- (b) CBD: Since October 1984 a consultant on external debt has been assisting the Ministry of Finance. The Central Bank has been assisted by a research advisor since August 1985, and a training advisor since December 1985, both of whose assignments were terminated in 1986.
- (c) Other: A Bureau of Statistics mission reviewed in May 1985 the coverage, sectorization, and classification of monetary accounts. In June 1986 technical assistance for the auction market was provided by a staff member from ETR.

XI. Resident Representative/Advisor:

Mr. Salvatore Schiavo-Campo assumed his post as resident representative to Somalia on March 27, 1985.

Table 1. Financial Relations of the World Bank Group with Somalia

Date of membership, IBRD: August 31, 1962  
 Capital subscription, IBRD: SDR 18.9 million

	Total credits <u>1/</u>	Disbursed <u>2/</u> and outstanding	Undisbursed <u>3/</u>
<hr/>			
<u>IDA credits</u> <u>4/</u>	(In millions of U.S. dollars)		
Agriculture, livestock, fisheries and rural development	170.1	89.4	80.3
Of which: ASAP <u>5/</u>	(66.7)	(14.6)	(52.1)
Education and technical assistance	31.5	28.3	2.8
Energy	27.2	19.7	7.5
Industry	4.5	4.5	--
Transportation	99.3	70.1	27.0
Utilities	21.0	15.0	1.1
Total	353.6	227.0	118.7
<u>IFC operations</u>	0.9	0.9	...

Source: World Bank.

1/ Original principal of outstanding credits, including valuation adjustments, less cancellations.

2/ Original principal, including valuation adjustments, less cancellations and repayments.

3/ Undisbursed credits, including valuation adjustments.

4/ Through November 30, 1986.

5/ Agricultural sector adjustment program.

Table 2. Somalia: World Bank Loans and Debt Service, 1983-88

(In millions of U.S. dollars)

	1983	1984	1985	1986	1987 <u>1/</u>	1988 <u>1/</u>
Loans	--	--	--	--	--	--
IBRD (net)	--	--	--	--	--	--
Disbursements	--	--	--	--	--	--
IDA (net)	17.0	24.6	21.8	47.8	43.5	41.9
Disbursements <u>2/</u>	(17.0)	(14.6)	(21.8)	(43.5)	(41.9)	41.9
Amortization	(--)	(--)	(--)	(--)	(--)	(--)
Total loans (net)	<u>17.0</u>	<u>24.6</u>	<u>21.8</u>	<u>47.8</u>	<u>43.5</u>	<u>41.9</u>
Interest payments						
IBRD	--	--	--	--	--	--
IDA	0.9	0.8	1.2	1.4	1.5	1.60
Total interest	<u>0.9</u>	<u>0.8</u>	<u>1.2</u>	<u>1.4</u>	<u>1.5</u>	<u>1.60</u>

Source: World Bank.

1/ Projections.

2/ Excludes Special Africa Facility disbursements of about US\$10 million in 1986, and US\$20 million and US\$25 million in 1987 and 1988, respectively. In FY 1987 IDA's Board of Executive Directors approved a Ports Modernization Project (US\$22 million), a Semi-Mechanized Rainfed Pilot Project (US\$13 million), and an Agricultural Extension Research Project for US\$12 million. For FY 1988, IDA envisage to bring to its Board three projects, namely for Power Rehabilitation (US\$10 million), Bardhere Dam Preparation (US\$10 million); and a 2nd Phase of the Agricultural Structural Adjustment Program (ASAP II) of about US\$50). For FY 1989 two projects are planned, including an Irrigation Rehabilitation Project on the Shebelli River for an amount of about US\$20 million, and the Bardhere Dam Multipurpose Project (irrigation, flood control, power generation and transmission) for US\$50. The total estimated cost for this last project is in excess of US\$350 million. For FY 1990 IDA envisages a project to rehabilitate Somalia's Public Sector Enterprises for which about US\$25 million has been earmarked. Also under active preparation is a Population/Health and Nutrition Project for US\$25 million, while a 3rd Phase of the Agricultural Structural Adjustment Program is scheduled for about US\$45.

SOMALIA--Basic Data

Area and population

Area 637,700 square kilometers  
Population: Total (mid-1985 estimate) 5.8 million  
Growth rate 3.1 percent

	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u> Prelim. Actual	<u>1986</u> Est.	<u>1987</u> Prog.
<u>GDP at factor cost</u> (at 1978 prices) <u>1/</u>						
Annual real rate of growth (percent)	8.5	2.4	3.5	6.4	5.0	4.1

Prices (percent change)

Mogadiscio consumer price index (period average)	22.6	36.4	92.2	37.8	35.6	18.7
---	------	------	------	------	------	------

Government finance

(In millions of Somali shillings)

Total revenue	2,588	4,075	3,774	5,220	9,500	12,700
Transfers from local authorities	172	178	205	...	...	...
Grants (excluding direct food aid for refugees)	1,056	1,106	1,980	6,620	10,418	27,948
Ordinary expenditure <u>2/</u>	-2,750	-4,539	-7,965	-9,918	-16,234	-17,951
Transfers to local authorities	-155	-177	-175	...	...	...
Investment expenditure	-2,461	-1,920	-3,124	-7,940	-10,433	-32,806
Overall deficit (-)	-1,550	-1,277	-5,305	-6,018	-9,146	-10,109
Change in domestic counterpart external arrears	—	—	1,800	-1,440	2,834	-1,898
Other adjustment to cash basis	...	...	...	300	...	...
Financing	1,550	1,277	3,505	7,158	6,312	12,007
Foreign (net) <u>3/</u>	1,724	1,572	940	5,033	6,426	4,530

1/ Somalia has no reliable series of national income data. These are staff estimates.

2/ 1985 and 1986 on commitment basis.

3/ Includes loans-in-kind.

## SOMALIA - Basic Data (concluded)

	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u> Prelim. actual	<u>1986</u> Est.	<u>1987</u> Prog.
<u>Government Finance (cont'd)</u> (In millions of Somali shillings)						
Domestic	-174	-295	2,565	1,045	-152	-500
Banking system	(-150)	(-295)	(2,573)	(875)	(-152)	(-500)
Cash balances	(-24)	(—)	(-8)	(170)	(—)	(—)
Debt relief	—	—	—	1,080	...	...
...						
Financing gap <u>1/</u>	...	...	...	...	...	7,977
<u>Money and credit (end of period)</u> (Percent change)						
Domestic credit	10.5	4.7	82.8	19.8	20.7	6.8
Government (net)	-6.7	-14.0	142.6	23.8	12.1	-8.2
Other	27.3	18.2	51.6	16.4	28.4	18.5
Money and quasi-money	14.4	7.1	22.4	45.4	37.0	13.1
<u>Balance of payments <u>2/</u></u> (In millions of U.S. dollars)						
Exports, f.o.b.	137	100	62	93	99	115
Imports, c.i.f. <u>3/</u>	-484	-450	-406	-367	-363	-404
Trade balance	-347	-350	-344	-274	-264	-289
Services and private transfers (net)	59	55	25	-35	-33	-24
Current account balance	-288	-295	-319	-309	-297	-313
Capital account (net)	244	209	180	259	210	317
Official <u>3/</u>	280	248	220	278	243	317
Private	-36	-39	-40	-19	-33	—
Allocation of SDRs	—	—	—	—	—	—
Overall deficit	-44	-86	-139	-50	-87	+5
<u>Gross official foreign reserves</u> (end of period)						
	14.3	15.8	6.3	11.6	26.6	34.6
In weeks of imports	1.5	1.8	0.8	1.6	3.8	4.5
<u>External public debt</u>						
Disbursed and outstanding <u>4/</u> (end of period)	856.2	958.5	1,023.3	1,229.7	1,277.7	1,340.7
Debt service as percent of exports of goods, non-factor services, and private transfers <u>4/</u>	...	...	57.2	68.3	93.2	94.8

1/ Expected to be closed through debt relief.

2/ On a commitment basis from 1985.

3/ Including loans and grants in kind.

4/ Excludes special bilateral agreements with the U.S.S.R. and Bulgaria, and loans from the People's Republic of China and Abu Dhabi that have been frozen by mutual consent.