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EBS/86/93

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April 24, 1986

To: Members of the Executive Board

From: The Secretary

Subject: Somalia - Review Under Stand-By Arrangement and Request for Waiver of Performance Criteria

Attached for consideration by the Executive Directors is a paper on the review under the stand-by arrangement for Somalia and its request for a waiver of the performance criteria. Draft decisions appear on pages 34-36.

This subject has been scheduled for discussion on Monday, May 12, 1986.

Mr. Jiménez (ext. 6952) or Mr. Simpson (ext. 6939) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

Att: (1)

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INTERNATIONAL MONETARY FUND

SOMALIA

Review Under Stand-By Arrangement and Request for Waiver of Performance Criteria

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

(In consultation with the Fiscal Affairs, Legal, and Treasurer's Departments)

Approved by G.E. Gondwe and W.A. Beveridge

April 23, 1986

I. Introduction

The present review of the current stand-by arrangement for Somalia was scheduled to have been completed before June 1985. Since April 1985, there have been continuous discussions with the Somali authorities, aimed at reaching understandings on the policies and measures, including performance criteria which would have allowed for completion of the review. Recently, considerable progress has been made in establishing this policy framework. A mission visited Mogadiscio between January 5-12, 1986, at which time a financial program was formulated. The Somali representatives included Mr. Hussein K. Afrah, Second Vice President and Minister of National Planning; Mr. Mohamed Sheikh Osman, Minister of Finance; Mr. Abdalla Mohamed Fadil, Minister of Commerce and Industry; Mr. Abdullahi Warsame Nur, Minister of Revenue; Mr. Omar Ahmed Omar, Governor of the Central Bank; and other senior officials dealing with economic and financial matters. The mission also met with H.E. Major General Mohamed Siad Barre, President of the Somali Democratic Republic. The staff representatives were Mr. J. M. Jiménez (head-AFR), Mr. J. Modi (FAD), Mr. M. Nowak (ETR), Ms. N. Calika (AFR), and Ms. M. Rubin (secretary-ETR). Mr. Y.H. Farzin (EA2NE-IBRD) also formed part of the mission. Mr. S. Schiavo-Campo, Resident Representative in Somalia, participated in the discussions. An additional staff visit took place between March 6-9, 1986.

On January 25, 1985, the Fund approved in principle Somalia's request for a one-year stand-by arrangement in an amount equivalent to SDR 22.1 million (50 percent of quota, EBS/85/1). The arrangement came into effect on February 22, 1985 after it had been determined that the 1985 balance of payments was fully financeable. At that time Somalia also made a purchase of SDR 32.6 million (equivalent to 73.8 percent of quota) under the compensatory financing facility (EBS/85/8), which had been approved earlier and had been contingent upon the coming into effect of the stand-by arrangement.

The program required special donor assistance for closing the estimated financing gap, in addition to the rescheduling of external debt service payments and arrears. To this end, a Special Donors Meeting was held in Paris on January 23, 1985, and a meeting of official creditors within the framework of the Paris Club was held on March 4, 1985. In addition, arrangements were made with some official creditors that did not participate in the Paris Club for additional debt relief.

So far, only SDR 2 million has been purchased under the stand-by arrangement. The purchase of SDR 3 million scheduled to be made in May 1985 on the basis of observance of the performance criteria for end-March was not made because Somalia accumulated new external debt service arrears in the first quarter. All subsequent purchases have been interrupted pending the reaching of understandings regarding the circumstances under which purchases can be resumed.

The authorities have requested that the period of the current stand-by arrangement be extended from its date of expiration of April 23, 1986 to September 30, 1986, to permit a fuller implementation of the objectives of the program. The Board agreed to the proposed extension of the arrangement. However, in view of the period of time in which upper credit tranche purchases under the arrangement were interrupted, understandings with the authorities provide for a reduction of the access during the extension of the arrangement from SDR 20.1 million to SDR 18.1 million. As a result, the remaining purchases under the current stand-by arrangement are to be rephased so that SDR 9.66 million will become available on completion of the review, a purchase of SDR 5.2 million on the basis of performance criteria for the end of April and a purchase of SDR 3.2 million on the basis of performance criteria for the end of June 1986. The latter two drawings will also be subject to the completion of a review on the financing of the balance of payments gap, exchange rate, budgetary policies, and petroleum pricing.

Since mid-1983, Somalia has experienced frequent difficulties in discharging its financial obligations to the Fund on schedule. At the end of 1985, arrears to the Fund amounted to SDR 13.6 million. A further SDR 7.4 million were accumulated through April 15, 1986. On December 27, 1985 the Fund adopted Decision No. 8164-(85/188)G/TR limiting Somalia's use of the general resources of the Fund until such time as Somalia becomes current on its financial obligations in the General Department. On March 26, 1986 the Fund reviewed Decision No. 8164-(85/188)G/TR and agreed to review it again no later than June 25, 1986. Meanwhile, the Government has made arrangements to clear all of its arrears to the Fund in April 1986. As of the end of 1985, Fund holdings of Somalia shillings, subject to repurchase, amounted to SDR 129.4 million (292.9 percent of quota) or excluding purchases under the CFF, SDR 96.9 million (219.1 percent of quota) (Table 1). Assuming that all purchases under the existing arrangement are made, Fund holdings of Somalia sh

Table 1. Somalia: Use of Fund Credit, 1985-86

	Outstanding at beginning of arrangement Dec. 31, 1984	1985 Jan.-March	1985 Apr.-June	1985 Jul.-Sept.	1985 Oct.-Dec.	1986 Jan.-May	1986 June-July	1986 Aug.-Sept.
				(In millions of SDRs)				
Transactions under tranche policies (net)		-1.98	-2.32	-0.61	-1.89	-7.80	-0.41	1.63
Purchases 1/		2.00	--	--	--	9.66	5.22	3.22
Ordinary resources		(1.00)	(--)	(--)	(--)	(4.83)	(2.61)	(1.61)
Borrowed resources		(1.00)	(--)	(--)	(--)	(4.83)	(2.61)	(1.61)
Repurchases		3.98	2.32	0.61	1.89	17.46	5.63	1.59
Credit tranche		(2.07)	(1.58)	(0.61)	(0.97)	(11.70)	(2.91)	(1.59)
Enlarged access		(1.91)	(0.74)	(--)	(0.92)	(5.76)	(2.72)	(--)
Transactions under special facilities (net) 3/		32.60	--	--	--	--	--	--
Purchases		32.60	--	--	--	--	--	--
Repurchases		--	--	--	--	--	--	--
Total Fund credit outstanding (end of period)	103.64	134.26	131.94	131.33	129.45	121.65	121.24	122.87
Under tranche policies	103.64	101.66	99.34	98.73	96.85	89.05	88.64	90.27
Under special facilities	--	32.60	32.60	32.60	32.60	32.60	32.60	32.60
				(As percent of quota)				
Total Fund credit outstanding (end of period)	234.48	303.76	298.53	297.14	292.88	275.23	274.30	277.99
Under tranche policies	234.48	230.00	224.75	223.37	219.12	201.47	200.54	204.23
Under special facilities	--	73.76	73.76	73.76	73.76	73.76	73.76	73.76

Sources: Treasurer's Department; and staff estimates.

1/ Purchases equivalent to SDR 3 million for May 1985, SDR 5.70 million for August 1985, SDR 5.7 million for November 1985, and SDR 5.7 million for February 1986 were not made because Somalia did not meet all performance criteria, and the review of the stand-by arrangement was not completed on schedule.
2/ Compensatory financing facility.

The staff report on the last Article IV consultation with Somalia was discussed by the Executive Board on August 9, 1985 (SM/85/203, and Supplement 1). Somalia continues to avail itself of the transitional arrangements of Article XIV.

II. Background

After having successfully implemented two arrangements in the period 1981-83, the Government held back in implementing a third program in 1984, as it felt that a more gradual adjustment approach was appropriate in view of existing social and political circumstances. In the event, financial policies became expansionary in 1984, and this, combined with adverse external factors, including the continuing ban on Somali cattle imports by Saudi Arabia, resulted in a sharp deterioration in internal and external imbalances and a major resurgence of inflationary pressures. The economy was affected by a major shortage of foreign exchange and essential imported inputs, in part fostered by speculation against the exchange rate. On the parallel market, there was a major depreciation of the exchange rate and the shortages of imported items led to the reintroduction of the franco valuta system, reinforcing speculation against the exchange rate. Although economic growth is estimated to have remained at the previous year's level of about 2 percent, inflation reached 82 percent in 1984 (December/December) and was about three times the average rate of the previous three years.

Domestic revenue fell by about 8 percent, while total expenditures rose by 70 percent. Consequently, on a commitment basis, the overall budgetary deficit, including grants, in 1984, reached the equivalent of 6.9 percent of GDP compared to 3.3 percent in the previous year, and domestic bank financing rose to the equivalent of 3.4 percent of GDP, compared to reductions in net bank financing in the previous two years, averaging about 0.6 percent of GDP. A substantial portion of the overall deficit, equivalent to 2.3 percent of GDP, was financed by a net increase in external arrears (Table 2).

Net domestic credit from the banking system rose by nearly 83 percent in 1984, in part reflecting the large increase in credit to the Government, but also a 52 percent increase in credit to the rest of the economy. Broad money rose by 26 percent, compared to an average of 12 percent in the previous two years.

In 1984 livestock exports totalled only US$33 million, compared to US$72 million in 1983, and US$106 million in 1982, in part as a result of the cattle import ban in Saudi Arabia. There was also a major increase in scheduled debt service payments, with the debt service ratio rising sharply. These developments were quickly reflected in intense balance of payments pressures, which led to a rundown in gross official reserves at the start of the year and to an inability of Somalia to continue to make debt service payments on schedule.

Table 2. Somalia: Selected Economic and Financial Indicators, 1982-86

	1982	1983	1984 1/ Prel. est.	1985 2/ Prog.	1985 3/ Est.	1986 Prog.
	(Growth rate in percent unless otherwise specified)					
National income and prices						
GDP at constant prices	11.2	2.4	2.3	4.0	4.0	4.0
Consumer price index						
Average	22.6	36.4	92.2	20.0	37.8	...
December/December	30.9	48.9	82.0	...	30.4	22.0
Trends in central government finance						
Revenue	15.0	57.5	-7.6	92.9	37.7	60.1
Total revenue and grants	41.4	40.4	11.0	121.7	97.6	85.4
Total expenditure	44.2	23.7	69.7	43.3	43.1	76.1
Trends in monetary aggregates 4/						
Money and quasi-money	15.7	7.5	26.0	17.4	8.3	11.1
Net domestic credit	10.8	4.6	79.2	6.7	28.7	12.9
Government (net)	-3.4	-5.8	46.8	0.6	15.9	-4.2
Private	14.2	10.4	32.4	6.0	12.8	17.1
Interest rates						
Commercial bank lending rate						
Minimum	12.0	12.0	12.0	15.0	15.0	19.0
Maximum	14.5	14.5	14.5	20.0	20.0	24.0
Commercial bank maximum deposit rate	11.0	11.0	11.0	18.0	18.0	22.0
Trends in external sector (in U.S. dollars)						
Exports, f.o.b.	20.2	-27.0	-38.0	81.7	72.6	21.5
Imports, c.i.f.	14.7	-7.0	-9.8	24.7	-1.5	6.3
Nominal effective exchange rate (depreciation -)	-27.3	-11.3	-9.0	...	-46.0 5/	...
Real effective exchange rate (depreciation -)	-20.8	10.5	60.4	...	-31.2 5/	...
	(In percent of GDP)					
Overall budget balance						
Including grants	-5.5	-3.3	-6.9	-2.0	-3.9	-4.5
Excluding grants	-9.3	-6.1	-9.5	-8.9	-9.8	-13.8
Current budget balance						
Including grants	3.3	1.6	-2.8	6.7	2.4	7.5
Excluding grants	-0.5	-1.2	-5.4	-0.2	-3.5	-1.8
Balance of payments 6/						
Current account balance	-9.0	-12.9	-11.9	-10.0	-11.0	-11.8
Current account balance, excluding official grants	-19.8	-24.7	-26.3	-30.6	-23.8	-24.2
Overall balance	-3.6	-9.0	-11.5	-2.8	-5.3	-8.2
	(In millions of U.S. dollars unless otherwise specified)					
Current account balance	-131.0	-162.0	-145.0	-131.0	-143.0	-169.0
Current account, excluding official grants	-288.0	-310.0	-319.0	-400.0	-311.0	-347.0
Overall balance of payments	-53.0	-113.0	-139.0	-37.0	-70.0	-117.0
Gross official reserves	14.0	16.0	6.0	39.0	8.0	12.0
(in weeks of cash imports)	(3.6)	(4.0)	(2.0)	(9.2)	(3.7)	(4.4)
External debt, including IMF	1,146.4	1,260.5	1,348.0	1,446.8	1,693.0	1,872.0
Debt service ratio	9.5	13.2	58.1	27.2	55.0	61.1
External debt servicing arrears	55.6	82.8	113.9	--	46.4	28.4
External commercial arrears	...	...	33.0	10.0	0.2	0.2

Sources: Data provided by the Somali authorities; and staff estimates. GDP data are based on staff estimates derived from 1978 base using estimates of real GDP growth and the consumer price index as a proxy for the GDP deflator.

1/ Balance of payments data for interest and amortization payments, as well as debt service ratio, are on commitment basis.
2/ The fiscal and monetary data exclude the resources accruing to the Government as a result of the gap-fill exercise.
3/ *The fiscal and monetary data include the resources accruing from the gap-fill exercise.*
4/ 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.
5/ January-November 1985.
6/ GDP in Somali shillings converted to U.S. dollars at rates necessary to maintain the purchasing power parity at 1973 level.

The foreign exchange shortages were reflected in a rise in the parallel market exchange rate; by end 1984, the parallel market rate had reached So. Sh. 80-100 per U.S. dollar, compared to an official exchange rate of So. Sh. 26 per U.S. dollar (Chart 1). A fuller description of 1984 developments is found in EBS/85/1 (1/2/85) and SM/85/203 (7/15/85) and Supplement 1 (8/8/85).

III. Developments in 1985

The authorities began the year with gross reserves virtually depleted, a large amount of payments arrears, mounting debt service payments, and a continued bleak outlook for export earnings. Shortages of imports had begun affecting the productive sectors of the economy, and there continued to be mounting pressures on the exchange rate. The inflation rate remained high, and there was a need to reduce the overall budgetary deficit and the credit expansion. To correct these problems, the authorities embarked on a comprehensive economic and financial program in 1985, aimed not only at reducing the external and internal imbalances, but also at raising the rate of economic growth, reducing the rate of inflation, and attaining external viability over the medium term. The program sought to readjust costs and prices to reflect market conditions more accurately. In addition, the authorities were to press forward with the reform of public enterprises and the implementation of an expanded public investment program, while tightening financial policies and adjusting the interest rate structure. Additional donor support was to be harnessed, not only through a rescheduling of external debts, but through additional capital flows, principally in the form of cash or petroleum products. A summary of the program is provided in Table 3.

The objectives set out by the authorities were ambitious and relied heavily on the proper timing of adjustment measures and external support. Given the low level of gross official reserves, the margin of maneuver was small.

On January 1, 1985, the Somali authorities introduced a market-determined exchange rate for most private transactions. An official exchange rate was maintained on a transitional basis for government transactions and for the surrender requirement of export proceeds, which was reduced from 100 percent to 35 percent. The official exchange rate was also devalued at that time, by 28 percent in foreign currency terms, to So. Sh. 36 per U.S. dollar, and it was to be adjusted during the year, so that it would become unified with the free market rate by the end of 1985.

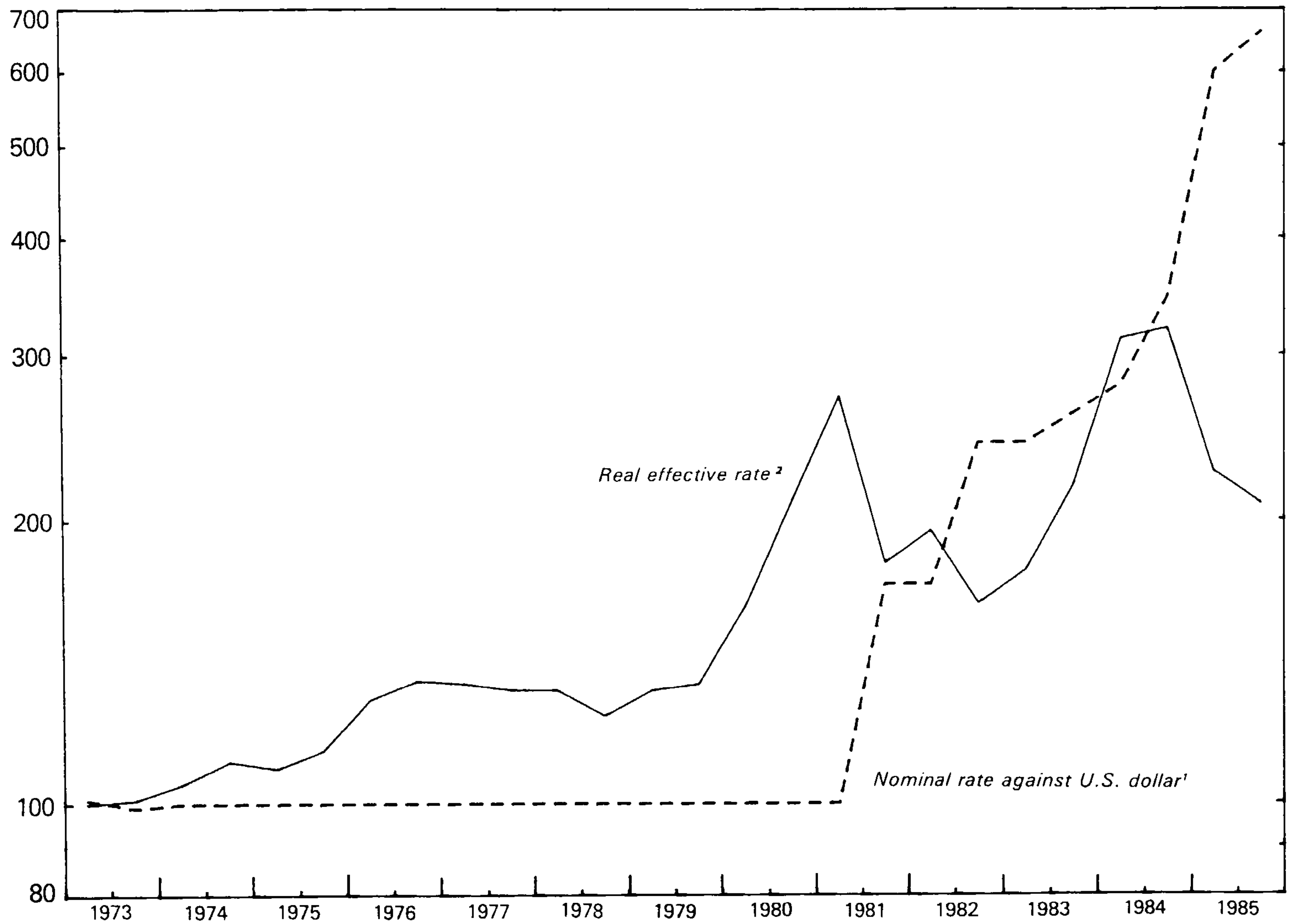
As an integral part of the exchange reform, the authorities liberalized and simplified the exchange and trade system. Generally, residents and nonresidents are free to buy and sell foreign exchange, practically all controls with respect to trade and current payments have been removed, and most notably, licensing requirements for virtually all

CHART 1

SOMALIA

EXCHANGE RATE INDICES

(1973 = 100, period averages)



Source: IMF Data Fund.

[1]Increase in index denotes depreciation against U.S. dollar.

[2]Increase in index denotes real effective appreciation.

Table 3. Somalia: Implementation Status of 1985 Financial Program

Program	Implementation status at end-1985
1. External sector policy	
a. Adopt a freely floating system for the determination of the exchange rate for most private transactions.	Implemented.
b. Devalue the official exchange rate by 28 percent in foreign currency terms on January 1, 1985 and peg the rate to the real SDR plus an additional adjustment of So. Sh. 0.5 per U.S. dollar per month through June 1985.	Implemented at the minimum acceptable level for the exchange regime adopted. The June adjustment to the rate made in November 1985.
c. Adjust the commercial bank posted exchange rate to reflect the market exchange rate.	Not implemented. From April to December no adjustment made in the rate.
d. Discontinue the franco valuta system.	Implemented.
e. Establish guideline prices for livestock exports.	Not implemented.
f. Eliminate virtually all trade restrictions.	Implemented.
g. Unify the official exchange rate with the market exchange rate at end-1985.	Not implemented.
h. Discontinue the bonus scheme.	Implemented.
i. Formalize verbal agreements on debt relief by mid-1985.	Not implemented.
j. Eliminate end-1984 external debt service payments arrears by mid-1985.	Not implemented. New external arrears accumulated.
k. Secure resources to cover the financing gap for 1985.	Somalia participated in special Donor Meeting and Paris Club rescheduling. Donor assistance, however, was not in the form envisaged in the program. Moreover, bilateral agreements in conformance to Paris Club rescheduling not completed by end-June 1985.

Table 3. Somalia: Implementation Status of 1985 Financial Program (continued)

Program	Implementation status at end-1985
l. No new commitments for public and publicly guaranteed nonconcessional external debt with a maturity of 1-12 years.	Implemented.
m. Accumulate no new short-term debt other than normal trade-related credits.	Implemented.
n. Improve external debt management and data base.	Implemented.
o. Reduce nongovernment commercial arrears by one-half during 1985.	Implemented.
2. <u>Fiscal policy</u>	
a. Reduce the overall deficit on commitment basis to So. Sh. 2 billion (2.0 percent of GDP).	Not implemented. Overall deficit on commitment basis reduced only to So. Sh. 4.4 billion (3.9 percent of GDP).
b. Confine expansion in net domestic credit to 1.3 percent.	Not implemented. Net domestic credit to to Government estimated to increase by 23.8 percent.
c. Convert all specific excise taxes to <u>ad valorem</u> basis.	Not fully implemented.
d. Abolish the 50 percent surcharge on imports through external accounts and apply 20 percent surcharge to nongovernment imports.	Implemented.
e. Apply custom duties on basis of prices in letters of credit or up-to-date price lists, whichever is higher. Use the market exchange rate for the conversions.	Not fully implemented. The exchange rate used to determine import duties was set at So. Sh. 60 = US$1.
f. Apply income tax to public enterprises and abolish turnover tax, share of profit tax, and charges on depreciation of public enterprises.	Not implemented.

Table 3. Somalia: Implementation Status of 1985 Financial Program (continued)

Program	Implementation status at end-1985
g. Introduce structural and administrative reforms to improve tax collection.	Implemented. A new ministry established to increase revenue.
h. Establish an information management unit to modernize and reform the budget system.	Not implemented.
i. Confine civil service salary increases to an average of 15 percent.	No salary increase given. However, benefits in kind amounting to So. Sh. 1.2 billion given to civil servants, armed forces, etc.
j. Reduce civil service employment by 2 percent.	Implemented.
k. Limit allocations for administrative expenses and contingency fund.	Implemented.
l. Confine investment expenditures to a level consistent with available concessional financing.	Implemented.
3. <u>Monetary policy</u>	
a. Reduce monetary growth to 17 percent in 1985.	Not implemented. Total monetary liabilities increased by 48.6 percent.
b. Limit the expansion in domestic credit to 6.7 percent of beginning money stock.	Not implemented. Net domestic credit increased by 27.1 percent of beginning money stock.
c. Increase interest rate structure and keep the structure under review to ensure positive real interest rates at end-1985.	Not fully implemented. Interest rate structure increased at beginning of 1985 but then not revived so that at end-1985 real interest rates were negative.
d. Complete study on reforming banking system by mid-1985 and begin implementing recommendations of study.	Not implemented.
4. <u>Pricing and marketing policies</u>	
a. Dismantle officially all price controls.	Implemented.

Table 3. Somalia: Implementation Status of 1985 Financial Program (concluded)

Program	Implementation status at end-1985
5. Public enterprises	
a. Prepare breakdown of public enterprises into those which should be phased out of operation, privatized, or retained in public sector.	Not implemented.
b. Set up timetable to reform public enterprises.	Not implemented.
c. Continue instituting boards of directors at public enterprises.	Implemented.

Source: Letter of intent, EBS/85/1, and information provided by the Somali authorities.

import and export transactions have been abolished. In addition, external payments arrears were programmed to be virtually eliminated, either through cash payments or through rescheduling arrangements.

Balance of payments developments during the year fell considerably short of expectations, with significant adverse impact on the rest of the economy. The only favorable development was the strong performance of exports, which was prompted in part by the new exchange arrangement. Exports are now estimated at US$107 million (Table 4). The inflow of grants and loans fell considerably short, however, of the targeted amounts. There were significant shortfalls in both private and official transfers which are now estimated at US$201 million, or some 42 percent below the estimate included in the program. The former has been greatly affected by the changing employment opportunities in the neighboring oil exporting countries. The current account deficit is estimated at 5.1 percent of GDP, compared to 3.8 percent in 1984 and a target of 6.2 percent. Net capital inflows, at US$74 million, were less than half the amount anticipated in the program. At the same time, net service payments were considerably higher than initially projected. As a result of these developments, actual imports are now projected at only US$400 million, or only 70 percent of the estimate included in the program. While there were shortfalls in all categories of imports, both tied and untied, the greatest shortfall was incurred in cash imports, as these totalled only US$111 million, compared to a target in the program of US$220 million. The balance of payments developments had considerable negative impact on the rest of the economy, particularly in the first half of the year, when the shortfall of capital inflows was greater than for the year as a whole. As a result, the Government of Somalia was unable to repay external arrears as programmed in the first half of the year, and consequently, failed to meet the relevant performance criteria. Despite the rescheduling of arrears and some repayments, new arrears estimated at US$34 million were incurred in 1985.

The foreign exchange availability was affected by a wait-and-see attitude of private individuals who delayed repatriating export and other earnings. Consequently, during this time, the economy suffered from a critical shortage of necessary imports, particularly petroleum products.

The revenue performance in 1985 was less strong than programmed reflecting both exogenous factors (i.e., reduced imports) and policy slippages. Revenue rose by 38 percent over the 1984 level, but fell slightly in relation to GDP and was 32 percent below the program target (Table 5). The shortfall in imports from the programmed level had a particularly negative impact on revenue collection, as cash imports, i.e., those that attract the highest duties, suffered the greatest shortfalls. Other major tax categories also recorded lower collection than estimated. Even though grants were 97 percent of the estimated level, during the year there were severe shortages because of delays by donors in releasing counterpart funds accumulated from the commodity import

Table 4. Somalia: Balance of Payments, 1982-86

(In millions of U.S. dollars)

	1982	1983	1984	1985 Prog. 1/	1985 Est.	1986 Proj. 1/	1986 Prog.
Current account	-131	-162	-145	-131	-143	-110	-169
Exports, f.o.b.	137	100	62	109	107	127	130
Livestock	(106)	(72)	(33)	(78)	(77)	(91)	(95)
Bananas	(14)	(15)	(14)	(14)	(13)	(16)	(15)
Others	(17)	(13)	(15)	(17)	(17)	(20)	(20)
Imports, c.i.f.	-484	-450	-406	-570	-400	-546	-425
Cash	(-204)	(-206)	(-156)	(-220)	(-111)	(-180)	(-142)
Grants-in-kind	(-157)	(-147)	(-151)	(-229)	(-127)	(-243)	(-158)
Loans-in-kind	(-123)	(-97)	(-99)	(-121)	(-162)	(-123)	(-125)
Trade balance	-347	-350	-344	-461	-293	-419	-295
Services (net)	9	-11	-47	-19	-51	-48	-82
Interest payments	(-14)	(-21)	(-44)	(-31)	(-43)	(-45)	(-79) 2/
Other	(23)	(10)	(-3)	(12)	(-8)	(-3)	(-3)
Transfers	207	199	246	349	201	357	208
Private	(50)	(51)	(72)	(80)	(33)	(84)	(30)
Official	(157)	(148)	(174)	(269)	(168)	(273)	(178)
Capital account	78	49	6	94	74	76	52
Official (net)	114	88	46	94	114	71	62
Inflows	(132)	(107)	(106)	(121)	(162)	(123)	(136)
Outflows	(-18)	(-19)	(-60)	(-27)	(-48)	(-52)	(-74)
Private 3/	-36	-39	-40	--	-40	5	-10
Overall balance	-53	-113	-139	-37	-70	-34	-117
Financing	53	113	139	37	70	34	117
Central Bank	64	47	13	-3	30	-33	-11
Reserves	(28)	(-1)	(9)	(-33)	(-2)	(--)	(-4)
IMF (net)	(34)	(44)	(-3)	(35)	(32)	(-20)	(-5)
Other	(2)	(4)	(7)	(-5)	(--)	(-13)	(-2)
Commercial bank	-20	39	29	--	-16	--	12
Arrears	9	27	71	-61	-100	-27	-18
Debt relief	--	--	26	46	156	--	--
Current debt service	(--)	(--)	(--)	(22)	(47)	(--)	(--)
Arrears	(--)	(--)	(26)	(24)	(109)	(--)	(--)
Financing gap	--	--	--	55	--	94	134
Memorandum items:							
Gross reserves (in weeks of cash imports)	4	4	2	9	4	6	4
Current account/GDP (in percent)							
Adjusted 4/	-9.0	-12.9	-11.9	-10.1	-11.0	...	-11.8
Unadjusted	-5.0	-6.5	-3.8	-6.2	-5.1	...	-8.4

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

1/ Projections contained in EBS/85/203 and Supplement 1.
2/ Includes US$18 million in moratorium interest on 1985 debt relief.
3/ Includes valuation adjustment and net errors and omissions.
4/ GDP in Somali shillings converted at U.S. dollar rate necessary to maintain purchasing power parity at 1973 level.

Table 5. Somalia: Summary of Central Government Operations, 1982-86

Fiscal Year Ending December 31	1982	1983	1984 Prel. est.	1985 Program 1/	1985 Preliminary actuals 2/	1986 Staff est. before program 3/	1986 Program 4/
			(In millions of Somali shillings)				
Total revenue and grants	3,816	5,359	5,951	14,549	11,758	16,550	21,800
Revenue	2,588	4,075	3,766	7,574	5,185	6,550	8,300
Tax	(2,275)	(3,371)	(2,973)	(6,870)	(4,450)	(5,650)	(7,400)
Import duty	1,275	2,198	1,870	4,893	3,200	3,600 5/	5,350 6/
Export duty	123	124	37	250	100	150	150
Other taxes	877	1,049	1,066	1,727	1,150	1,900	1,900
Nontax	(313)	(704)	(793)	(704)	(735)	(900)	(900)
Grants 7/	1,056	1,106	1,980	6,760	6,573	10,000	13,500
Oil grant and commodity import program	(600)	(901)	(620)	(2,760)	(2,504)	(2,800)	(4,785)
Transfers from local authorities	172	178	205	215	...	...	...
Total expenditure 8/	5,366	6,636	11,264	16,524	16,123	24,500	28,400
Ordinary expenditure	2,750	4,539	7,965	7,700	9,047	9,200	10,900
Wages and salaries	(...)	(...)	(2,150)	(...)	(2,152)	(2,200)	(2,200)
Interest: Domestic	(...)	(...)	(385)	(...)	(360)	(400)	(400)
Foreign	(...)	(...)	(540)	(...)	(1,167) 9/	(1,500)	(2,300)
Other expenditure	(...)	(...)	(4,890)	(...)	(5,368)	(5,100)	(6,000)
Investment expenditure	2,461	1,920	3,124	8,560	7,076	15,300	17,500
Development budget	(348)	(498)	(604)	(1,200)	(1,504)	(2,113)	(2,113)
Transfers to local authorities	155	177	175	264	...	...	...
Overall deficit on commitment basis							
Excluding grants	-2,606	-2,383	-7,293	-8,735	-10,938	-17,950	-20,100
Including grants	-1,550	-1,277	-5,313	-1,975	-4,365	-7,950	-6,600
Change in domestic counterpart external arrears (excluding debt relief)	--	--	1,800	-1,840	-1,440	-450	-800
Overall deficit on cash basis	-1,550	-1,277	-3,513	-3,815	-5,805	-8,400	-7,400
Financing	1,550	1,277	3,513	3,815	5,805	8,400	7,400
Foreign (net)	1,724	1,572	940	3,760	3,680	2,400	4,700
Domestic	-174 10/	-295	2,573	55	1,045	6,000	-300
Banking system (net)	*(-174)*	*(-295)*	*(2,573)*	*(55)*	*(1,045)*	*(6,000)*	*(-300)*
Debt relief	--	--	--	--	1,080 11/	--	...
Financing gap	--	--	--	--	--	--	3,000 12/
			(In percent of GDP)				
Total revenue and grants	13.6	13.7	7.8	14.9	10.5	11.4	15.0
Of which: revenue	(9.3)	(10.4)	(4.9)	(7.7)	(4.6)	(4.5)	(5.7)
Total expenditure	19.2	17.0	14.7	16.9	14.4	16.8	19.5
Ordinary expenditure	(9.8)	(11.6)	(10.4)	(7.9)	(8.1)	(6.3)	(7.5)
Investment expenditure	(8.8)	(4.9)	(4.1)	(8.8)	(6.3)	(10.5)	(12.0)
Transfers to local authorities	(0.6)	(0.5)	(0.2)	(0.3)	(...)	(...)	(...)
Overall balance							
Excluding grants	-9.3	-6.1	-9.5	-8.9	-9.8	-12.3	-13.8
Including grants	-5.5	-3.3	-6.9	-2.0	-3.9	-5.4	-4.5
Change in arrears	--	--	2.3	-1.9	-1.3	-0.3	-0.6
External financing (net)	6.1	4.0	1.2	3.8	3.3	1.7	3.2
Bank financing (net)	-0.6 10/	-0.7	3.4	0.1	0.9	4.1	-0.2
Debt relief	--	--	--	--	1.0	--	--
Financing gap	--	--	--	--	--	--	2.1
GDP in current prices	27,972	39,070	76,820	97,762	111,850	145,405	145,405

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

1/ Based on an average official exchange rate of So. Sh. 40 per U.S. dollar assumed in the program.
2/ Based on an average exchange rate of So. Sh. 39.50 per U.S. dollar.
3/ Based on an average official exchange rate of So. Sh. 42.5 per U.S. dollar.
4/ Based on an average exchange rate of So. Sh. 72.5 per U.S. dollar.
5/ Based on the valuation of imports at So. Sh. 60 per U.S. dollar.
6/ Based on the valuation of imports at commercial exchange rate.
7/ Includes cash grants (as well as grants-in-kind), including project grants, Saudi oil grant, commodity import program, and budgetary support in the form of food aid.
8/ Commitment basis.
9/ Includes interest payable of So. Sh. 440 million ($11 million) which was subsequently rescheduled at the Paris Club meeting of March 1985.
10/ *Includes use of cash in Treasury vaults amounting to So. Sh. 24 million.*
11/ Consists of the debt relief on amortization of So. Sh. 640 million ($16 million) and of So. Sh. 440 million ($11 million) on interest due.
12/ Expected to be closed through debt relief on interest payments of So. Sh. 435 million ($6.1 million, which is net of the payment of interest moratorium of $18.7 million) and on amortization of So. Sh. 2,560 million ($35.2 million).

programs. Despite these difficulties, total revenues and grants reached the equivalent of 10.5 percent of GDP, compared with 7.8 percent in 1984, but were lower than the target in the program of 14.9 percent. The authorities were concerned about the weak revenue performance, and during the year, they attempted not only to counteract lower revenue collections by reducing expenditure, but also, in August 1985, formed a new Revenue Ministry, with the explicit objective of improving the administration of revenue collections.

Total expenditure on a commitment basis was limited to So. Sh. 16.1 billion, 2.4 percent below the level included in the program. Within this amount, however, ordinary expenditure exceeded the programmed level by So. Sh. 1.3 billion or about 17 percent. The program had expected ordinary expenditure to fall during the year. The higher level of ordinary expenditure reflected in part foreign exchange losses incurred by the Government in purchasing foreign exchange in the free market, a higher level of interest payments, and some supplementary appropriations, including So. Sh. 1.2 billion in benefits-in-kind from the commodity import programs to employees of certain government institutions, So. Sh. 1.1 billion of a nonrecurring nature comprising the completion of certain projects for which foreign financing was cut due to debt service arrears, an increased subscription to the capital of the Somali Development Bank, the higher cost of government imports, and additional provisions for debt servicing. Apart from these items, the Government followed a tight wage policy, keeping total wages and salaries and other expenditures, principally for goods and services, virtually at the 1984 level and below the programmed level with a saving of So. Sh. 1.0 billion. These actions were only accomplished with difficulty and have resulted in real wages in the public sector falling substantially, thereby limiting the efficiency of public administration. Investment expenditure was limited to So. Sh. 7.1 billion, compared with a target in the program of So. Sh. 8.6 billion, and was more than double the 1984 level. An important part of the increase reflects the depreciation of the currency. The authorities made a particularly strong effort in the closing months of 1985 to keep the overall deficit close to the programmed level; however, despite their efforts, the overall deficit on a commitment basis, including grants, reached 3.9 percent of GDP, compared with a target of 2.0 percent in the program, and an actual level of 6.9 percent in 1984. Excluding grants, the deficit reached 9.8 percent of GDP, compared with 8.9 percent in the program and 9.5 percent in 1984. A smaller than programmed reduction in arrears and debt relief not provided in the program were partly offset by the shortfall in foreign loans. Domestic bank financing of the budget exceeded So. Sh. 1 billion, or 15 percent of the initial broad money stock, in comparison to a programmed small increase in bank financing. Nonetheless, in relation to the outcome of 1984, which utilized So. Sh. 2.6 billion in domestic financing, 1985 showed a significant improvement. Debt relief financed the equivalent of 1.0 percent of GDP.

Domestic credit policy was more expansionary in 1985 than projected in the program. This was influenced not only by the difficulties encountered in the external sector, but also by the higher level of inflation, the more rapid depreciation of the exchange rate than had been assumed, and the unfavorable budgetary performance. The program had assumed an increase in domestic credit of 6 percent, to So. Sh. 10.2 billion. However, domestic credit rose by 19.5 percent (Table 6). Net credit to the Government rose by 24 percent, compared with 143 percent in 1984, while credit to the rest of the economy increased by 16 percent, compared with 52 percent in 1984 and a program target of 10 percent. The expansion in net domestic credit, however, was smaller than nominal GDP. Domestic monetary liabilities to the private sector expanded by only 8.3 percent, compared with about 26 percent in 1984, while total monetary liabilities with the banking system expanded by 48.6 percent, compared with a target of 17.4 percent in the program. The larger increase in total monetary liabilities reflects the increase in foreign currency deposits by the private sector and their revaluation given the depreciation of the currency, and the buildup of counterpart funds from the foreign aid program.

Most of the difficulties in the external sector were reflected in the official exchange market. The substantial shortages which emerged in the official market, principally as a result of a failure to amalgamate the system sufficiently and shortfalls in foreign assistance, were reflected in an accumulation of new external payment arrears, a forced reduction of government imports, and a delay in transferring the budgetary allocations to Somali embassies abroad. The official market was also affected by reduced inflows from embassies and international institutions, which found that they required less foreign exchange to finance the local costs of development projects and their administrative expenses.

In December 1984, the parallel market rate was almost 3.5 times the official rate (Table 7). By the end of March the spread between the free market rate and the official rate had been reduced to 2.5 times and 2.4 by the end of June. In the period January-June 1985, the official exchange rate was adjusted from So. Sh. 36 per U.S. dollar to So. Sh. 40.6 per U.S. dollar. The weighted-average exchange rate in the free market rose from about So. Sh. 90 per U.S. dollar in December 1984 to So. Sh. 99 per U.S. dollar in June 1985. The free market rate rose to So. Sh. 115 by end-December 1985, while the official rate reached So. Sh. 42.5, widening the gap between the two rates and discouraging the repatriation of foreign exchange by Somali exporters, because of the surrender requirement at the lower official exchange rate.

A multiple currency practice also arose because the rate quoted by the Commercial Bank was not adjusted in line with the free market rate and has remained at So. Sh. 83.6 per U.S. dollar since April 1985.

Following the Paris Club meeting, Somalia had a deadline for concluding the bilateral agreements by June 30, 1985. At the end of 1985, only two of the bilateral agreements (France and the United States) had

Table 6. Somalia: Monetary Survey, 1982-86

	1982	1983	1984	1985		1986
	Dec.	Dec.	Dec.	Dec. Prog.	Dec. Est.	Dec. Prog.
	(In millions of Somali shillings)					
Net foreign assets 1/	468.9	-908.8	-2,330.2	-3,219.0	-2,730.4	-12,999.0
Central Bank	-959.1	-1,815.4	-2,929.9	-6,318.0	-5,996.8	-16,111.5
Commercial bank	1,428.0	906.6	599.7	3,099.0	3,266.4	3,112.5
Of which: Foreign currency accounts	(...)	(...)	(310.6)	(...)	(2,900.0)	(2,840.0)
Central bank accounts	(--)	(--)	(--)	(...)	(109.0)	(150.0)
(Net foreign assets in U.S. dollars)	(30.8)	(-51.8)	(-89.6)	(-53.7)	(-102.0)	(-113.0)
Domestic credit	5,024.0	5,260.8	9,616.2	10,150.0	11,496.0	12,411.0
Government (net)	2,100.1	1,805.0	4,378.1	4,448.0	5,421.0	5,121.0
Other	2,923.9	3,455.8	5,238.1	5,702.0	6,075.0	7,290.0
Monetary liabilities	5,116.1	5,500.9	6,933.2	10,081.0	10,299.6	11,367.0
Liabilities in local currency	5,116.1	5,500.9	6,547.2	...	7,090.6	7,877.0
Counterpart funds	...	...	75.4	...	200.0	500.0
Foreign currency deposits	...	...	310.6	...	3,009.0	2,990.0
(Foreign currency deposits in U.S. dollars)	(...)	(...)	(11.9)	(...)	(36.0)	(26.0)
Other items (net)	376.7	-1,148.8	352.8	-3,150.0	-1,534.0	-11,955.0
Valuation adjustment	-514.1	-1,551.6	-1,447.0	-7,397.0	-5,049.0	-20,840.0
Medium- and long-term foreign liabilities 2/	988.2	1,318.8	2,059.8	4,754.0	3,315.0	8,625.0
Other items (net)	-97.4	-916.0	-260.0	-507.0	200.0	260.0
	(Percentage increase from end of previous year) 3/					
Domestic credit	10.5	4.7	82.8	6.0	19.5	8.0
Government (net)	-6.7	-14.1	142.5	1.3	23.8	-5.5
Other	27.3	18.2	51.6	10.0	16.0	20.0
Monetary liabilities	15.7	7.5	26.0	17.4	48.6	10.4
Liabilities in local currency	...	...	...	...	8.3	11.1
Counterpart funds	...	...	...	...	165.3	150.0
Foreign currency deposits	...	...	...	...	868.8	-0.6

Sources: Data provided by the Central Bank of Somalia; the Commercial and Savings Bank of Somalia; and staff estimates.

1/ Exchange rates were So. Sh. 15.206 = US$1 at end-1982, So. Sh. 17.556 = US$1 at end-1983 and So. Sh. 26 = US$1 at end-1984. For program 1985, end-December rate was So. Sh. 60 = US$1 while the actual rates at end-1985 were So. Sh. 42.5 = US$1 for the Central Bank and So. Sh. 83.613 for the commercial bank. For end-1986 a unified rate of So. Sh. 115 = US$1 is assumed. Projections for end-1986 assume drawings amounting to US$15 million under a new Fund arrangement. Net foreign assets include valuation adjustments.

2/ Includes valuation adjustments.

3/ The changes for program 1985 are in terms of estimated end-1983 data in the program paper, EBS/85/1.

Table 7. Somalia: Exchange Rates, 1984-86 1/

		Official rate	Market rate	Parallel rate	Ratio of free market rate to official rate
		(Somali shillings per U.S. dollar)			
1984	Dec.	26.0	--	80-100 2/	3.5
1985	March	37.0	91.0	...	2.5
	June	40.6	99.0	...	2.4
	Sept.	40.6	101.4	...	2.5
	Dec.	42.5	115.0	...	2.7
1986	Jan.	54.5	120.0 3/	...	2.2 3/

Source: Data provided by the Somali authorities.

1/ End of period.
2/ Exchange rate dependent on quantity to be exchanged.
3/ Estimate.

Following the Paris Club meeting, Somalia had a deadline for concluding the bilateral agreements by June 30, 1985. At the end of 1985, only two of the bilateral agreements (France and the United States) had been finalized. It is foreseen that the other two (Italy and the United Kingdom) will be signed shortly. The main difficulties causing the delay concern the interest rate provisions and continued discussions with Italy aimed at converting some of the rescheduled loans into grants. The Paris agreement foresaw the establishment of a special account to facilitate the payment primarily of moratorium interest. The amounts to be put into this account through June 30, 1985 had been fixed and Somalia made the necessary payments. For the period after June 30, 1985, the amounts depended on the provisions of the bilateral agreements, especially the agreement with Italy. As these have not been finalized, no further payments have been made by Somalia into the special account.

The review of the program was delayed from its scheduled date of June 1985 because of the difficulties found in balancing the official foreign exchange market (which led to the accumulation of additional external arrears), a departure from the agreed budgetary and interest rate policies, delays in implementing public enterprise reforms, and a delay in adjusting the official exchange rate. The authorities felt that in view of the emerging shortfall in the flow of foreign assistance some of the targets in the program had become overambitious. Although the problems in the official exchange market and in the budget were in part caused by the lower capital inflows, the necessary supporting measures to minimize the impact of such inflows were not implemented. In particular, the official exchange rate was not depreciated fast enough, nor were sufficient purchases in the free market undertaken. In the fiscal sector the revenue performance was allowed to deteriorate markedly.

With the improvement in capital inflows in the second half of 1985 gradual agreement evolved in a revised timetable for the continued implementation of the agreed policies in the arrangement. In view of the lower capital inflows and the delayed implementation of supporting measures the achievement of the targets according to the programmed timetable was no longer feasible, but still appeared possible over a longer period which would allow the authorities more time to implement the needed measures and to improve the coordination between the Government and the various interested donor governments. It was felt that this could best be done without loss of crucial time, within the framework of the existing stand-by arrangement which was, therefore, extended through September 30, 1986. The program has been designed accordingly; its elements are described in the following section and are summarized in Table 8.

IV. Program for 1986

1. Introduction

In the attached letter, the Minister of Finance and the Governor of the Central Bank detail the main policy initiatives which will be undertaken under the current program. The authorities have also indicated

Table 8. Somalia: Summary of 1986 Financial Program

Objectives

1. Achieve a real rate of economic growth of at least 4 percent.

2. Reduce the rate of inflation to about 22 percent.

3. Confine the current account deficit to US$169 million and the overall balance of payments deficit to US$ 117 million.

Policy Measures

1. External sector policy

a. Devalue the official exchange rate 22 percent in foreign currency terms to So. Sh. 54.5 = US$1 in January 1986.

b. Depreciate the official exchange rate on a monthly basis to reach parity with the free market rate by end-1986.

c. Adjust the commercial bank posted exchange rate every ten days to reflect the exchange rate in the free market.

d. Increase the export surrender requirement to 50 percent.

e. Increase minimum export prices for livestock to reflect current market conditions.

f. Increase monthly gasoline and diesel prices to reach import parity for gasoline by April 1986 and for diesel by June 1986.

g. Follow through with requests or initiate new requests for debt rescheduling to reduce the financing gap for 1986.

h. Reduce the outstanding stock of end-1985 external payments arrears by at least US$8 million by end-February 1986, by US$9 million by end-June 1986, and by US$18 million for the year as a whole. To the extent that the envisaged flows of foreign exchange in the official market may fall short of the transactions (including the net reduction of arrears) to be financed in that market, the Government will purchase foreign exchange in the free market to meet the arrears reduction target.

i. Refrain from contracting, or guaranteeing, any nonconcessional external loans with a 1 to 12 year maturity or short-term credits during 1986, except up to US$24 million of short-term borrowing to make payments to the Fund.

Table 8. Somalia: Summary of 1986 Financial Program (concluded)

2. Fiscal policy

a. Confine the overall deficit on commitment basis (including grants) to So. Sh. 6.6 billion (4.5 percent of GDP), and excluding grants to So. Sh. 20.1 billion (13.8 percent of GDP).

b. Reduce net domestic credit to government by 5.5 percent.

c. To ensure the projected 60 percent increase in revenue collections:

change specific tax rates to ad valorem basis;

broaden the coverage of excise duties already in place;

base the calculation of import duties on the posted commercial bank exchange rate; and

continue with administrative improvements.

d. To limit the increase in total expenditure to 76 percent:

maintain an unchanged wage bill during the year, including payments of benefits-in-kind;

continue with reform of the civil service; and

allow investment outlays in conformance to the agreement reached with the World Bank on the public investment program and in line with available project and commodity assistance.

3. Monetary policy

a. Confine the growth in broad money to 11.1 percent.

b. Reduce the expansion in net domestic credit to 8 percent.

c. Increase the maximum interest rate on commercial bank deposits by 4 percentage points.

4. Public enterprises

a. Review with a World Bank mission possible strategies for continuing with the reform of public enterprises and as a consequence develop a strategy for speeding up such reform.

Source: Appendix II.

their interest in requesting a new stand-by arrangement at the expiration of the current one. In developing the framework for the extension of the program period, the staff has worked closely with the World Bank in estimating the balance of payments financing gap, in reviewing the public investment program, and in discussing the other elements of the program. To ascertain the timely and adequate inflow of foreign assistance, the World Bank is playing a key role through its Consultative Group procedures. A Consultative Group meeting for Somalia was held in early November 1985, at which time the public investment program (1986-89) and the projected financing gap in the balance of payments for 1986 were discussed and pledges obtained for its financing. In addition, the Government of Somalia has indicated to the Paris Club its intention to request a restructuring of maturities due in 1986.

At the end of the Consultative Group meeting, the World Bank determined that the amount of project and commodity assistance which had emerged was in excess of Somalia's requirements for 1986, but that there were important shortfalls in the amount of cash assistance and/or petroleum aid for the year as a whole. The final statement also called attention to the need for rescheduling by official creditors that did not participate in the Paris Club and for greater coordination of donors in financing only projects included in the core investment program approved by the Bank. Since then, the Bank and the Fund have had further contacts with donor governments, to ascertain that progress toward filling the financing gap is being made. Participants in the Consultative Group supported the objectives of the investment program. Consequently, for a number of years, Somalia should continue to benefit from large inflows of foreign assistance.

For 1986, the authorities are projecting a rate of economic growth of about 4 percent, and are aiming to reduce inflation further, from the estimated 30 percent in 1985 to about 22 percent in 1986. Given the expected larger inflows of assistance to the budget in shilling terms, particularly in grant form, the fiscal program for 1986 allows an expansion of the overall deficit on a commitment basis, including grants, to rise to 4.5 percent of GDP compared with an estimate of 3.9 percent in 1985, and to 13.8 percent of GDP from 9.8 percent in 1985, excluding grants. Taking into account the estimated impact of debt relief on the budget, there will be a large adjustment in its domestic financing component, leading to a small improvement in the government's position with the banking system. Monetary policy is to be tightened with domestic credit expected to rise by about 8 percent for the year as a whole, including a 5.5 percent reduction in credit to the Government and an expansion of credit to the rest of the economy of about 20 percent. Broad money is expected to grow substantially below the growth of nominal income; thereby aiding in the authorities' efforts to reduce inflationary pressures.

The current account deficit of the balance of payments is expected to expand to 8.4 percent of GDP, compared with a deficit of 5.1 percent in 1985. The balance of payments for 1986 contains a financing gap of about US$135 million which is expected to be met largely through debt rescheduling, additional donor assistance, a possible drawing under the Structural Adjustment Facility, and purchases in the free market by the Government. Despite the fact that the balance of payments is financeable on a calendar-year basis, Somalia will face considerable difficulties in the first half of this year in meeting scheduled payments and financing necessary import levels, if foreign assistance indicated at the Consultative Group meeting in November does not flow on a timely basis. These difficulties are likely to emerge early in the year in the official market and the authorities have committed themselves to make purchases in the free market and/or continue to transfer additional items to the free market so as to maintain the balance between the demand and supply of foreign exchange in the official market. On the basis of the experience in 1985, the medium-term balance of payments outlook, discussed in EBS/85/1, has been revised to reflect more realistic capital inflows. The exchange markets will be unified in the course of 1986.

The program includes the following performance criteria: (1) ceilings on domestic bank credit for April and June 1986, with a subceiling on net domestic credit to the Government; (2) a ceiling on the contracting and guaranteeing of any nonconcessional external loan with 1-2 year maturity or any short-term credits other than normal trade related credits; (3) a target for the reduction of external payments arrears; (4) the standard provisions relating to the exchange and trade system; and (5) a review of the arrangement prior to the end of June 1986. Given the usual delays experienced in the availability of data, the purchase based on end of April performance criteria is not likely to be made until late June, while the purchase on the basis of June performance criteria will take place in August.

2. External sector policies

The major policy decisions implemented in 1985 in the external sector will be strengthened in the course of 1986. The free foreign exchange market is to continue to function without official interference. The liberal export and import conditions will be maintained and price controls will continue to be avoided. The program aims at a net repayment of arrears during 1986 of a minimum of US$18 million. As a performance criterion US$8 million will be repaid by end-April 1986. These amounts exclude any overdue payments for which Somalia is seeking a rescheduling. The program also includes a mechanism to ensure that the commercial bank exchange rate and the exchange rate used for the valuation of import duties accurately reflect the free market exchange rate. This was not the case in 1985, when the commercial bank rate remained unchanged for long periods of time leading to a restrictive multiple currency practice.

In 1985 the exchange arrangements had a positive impact on exports, and their continuation, together with the contracts established for livestock exports, will permit another large expansion of total exports in

1986, to just under the high level recorded in 1982. Exports continue to be constrained by the Saudi ban on cattle imports from Somalia, and a lifting of this ban would have a further salutary effect on total exports. Somalia's herd is sufficiently large to permit for an even larger expansion.

The integration of the official and the free foreign exchange markets will be carried out during the year. First, some of the items included in the official market will be progressively transferred into the free market. The official foreign exchange rate will be depreciated on a monthly basis with the aim of reaching parity with the free market rate by the end of 1986. The surrender requirement on exports has been increased from 35 percent to 50 percent. As mentioned earlier, despite the increase in the surrender requirement, the Government is likely to still need to make purchases in the free market to maintain the official market in balance. On January 31, 1986, the official exchange rate was So. Sh. 54.5 per U.S. dollar, representing a devaluation in foreign currency terms of 22 percent from the end-1985 level; on February 24, 1986 the official exchange rate was devalued again, by 6.8 percent, to So. Sh. 58.5 per U.S. dollar and further to So. Sh. 62.5 per U.S. dollar on April 1, 1986. The rate will be depreciated by a minimum of So. Sh. 4 per month. The review of the arrangement in April will ascertain whether the unification objective can be met by the end of 1986 by maintaining the agreed rate of monthly depreciation of the official rate or whether the rate of depreciation would need to be accelerated.

To further simplify the exchange system, the authorities have also decided to adjust the commercial bank quoted exchange rate every ten days to reflect the exchange rate in the free market. Similarly, the commercial bank rate will be utilized for calculating import duties beginning in February. At the present time they are being calculated at an accounting rate of So. Sh. 60 per U.S. dollar. However, since the adjustment in the bank rate will only take place every ten days, the differential that may emerge with the free rate may result in a restrictive multiple currency practice for which temporary approval under Article VIII, sections 2(a) and 3, is being requested.

The authorities opted to increase the surrender requirement on exports as a way of reducing their direct purchases in the market. This was done in the belief that large purchases from time to time by the authorities were likely to disrupt market conditions and exert destabilizing pressures on the free exchange rate. The increase in the surrender requirement will have the effect of reducing exporters' net earnings. However, this is likely to be offset in part by the additional depreciation of the free market rate which will result from the reduced supply of funds arising from the increased surrender requirement. Studies carried out by a donor agency on the profitability of livestock exports have shown that exporters are making large windfall profits, given current prices and exchange rates. The authorities will also be adjusting the minimum export prices, which have not been altered since January 1984. The unrealistically low minimum prices have permitted livestock exporters to retain an important proportion of their earnings abroad. This latter measure will also have a positive impact on the budget, because the export tax is based on the minimum export price.

During 1985 the domestic prices of petroleum products were adjusted several times. At the end of December, gasoline prices were about 85 percent of import parity and diesel 64 percent. The program contemplates fixed adjustment which will bring gasoline to import parity by April 1986 and diesel by June, if petroleum is valued at $24 per barrel. The available indications, however, point to a much lower world market price, especially for the equivalent in petroleum products. Thus, in effect, the agreed fixed schedule has resulted in the attainment of import parity sooner. The authorities have already made a public announcement allowing private sector imports of petroleum products.

3. Fiscal policy

Budgetary revenues are projected to rise by 60 percent in 1986, compared with 38 percent in 1985. The better revenue performance is being influenced by the changing of specific taxes to an ad valorem basis (on tobacco, alcohol, sugar and matches) and the broadening of the coverage of excise duties introduced in 1985, but not fully implemented, with the inclusion of 30 additional items taxable at rates ranging from 5 to 30 percent. These two measures are expected to yield So. Sh. 400 million. Most importantly, the revenue performance will be affected by the higher import duty base previously mentioned, the higher minimum export prices for livestock, and administrative improvements which are emerging from the new Ministry of Revenue. The change in the import duty valuation itself should provide an increased yield of So. Sh. 1.7 billion, and, as previously mentioned, import duties will be favorably affected by the increase in cash imports. There has been an evident improvement in revenue collection since the Ministry of Revenue was formed in August 1985, and the projected increase in revenue seems possible, but will require continuous monitoring and, if necessary, additional measures. The revised projections for 1986 result in the revenue ratio to GDP rising to 5.7 percent, reversing the downward trend of the past two years, but still significantly below the levels reached in the early 1980s. Grants are expected to approximately double in terms of Somali shillings. About 35 percent of the increase reflects the change in valuation of grants at a higher exchange rate.

Total government expenditure is expected to increase by 76 percent, reflecting the more than doubling of investment expenditures. About 14 percent of the increase, however, represents a change in the valuation of these expenditures given the new exchange rate system. Investment expenditure is estimated to reach 12.0 percent of GDP, compared to 6.3 percent in 1985. The 1986 investment budget reflects the agreement reached with the World Bank on the public investment program. A large percentage of the projects are ongoing, with approximately 40 percent in agriculture and irrigation. Transport and communications absorb an additional 16 percent and water resources a further 13 percent. Small allocations, however, are given to education and health. The Government will exercise a tight ordinary expenditure policy, limiting its growth to only 20 percent, which will result in a fall in the ratio to GDP to 7.5 percent, from 8.1 percent in 1985. The level of ordinary expenditure must be viewed in relation to the large nominal increases which took place in 1984, the large nonrecurring expenditures undertaken in 1985, and the Government's objective to maintain the wage bill virtually unchanged in 1986, including the allocation for benefits in kind. This policy is likely to result in further reductions in the civil service as early retirements will continue to be stressed and vacancies will generally not be filled. In addition, some dismissals may be effected to allow for some selective wage increases.

There is likely to be a shortfall in investment expenditure, but this will be offset by lower project grants and capital inflows.

The rise in overall deficit on a commitment basis must be viewed in relation to the increased availability of concessional resources to support a considerably larger investment program, and the expected continued availability of such support in the medium term. An increasing proportion of the expected capital will come in the form of grants, thus the larger increase in the overall deficit excluding grants. The deficit has also been influenced by the revaluation of investment outlays given the new exchange arrangements. As presently formulated, the budget has a financing gap of about So. Sh. 3 billion (2.1 percent of GDP), but this amount is expected to be fully met by debt relief and will permit a small repayment to the banking system during the year. It is foreseen that Somalia will continue to benefit from large support for its investment program in the future years, and that, therefore, the overall deficit will remain at a high level, but that the budget will be fully financeable without need of domestic financing.

4. Money and credit policy

As part of the program the monetary authorities increased deposit rates by about 4 percentage points. This will bring the maximum deposit rate to about 22 percent, which is equal to the inflation rate projected for the year as a whole. This adjustment will also affect other domestic interest rates. In an effort to improve financial intermediation, the Government announced in 1985 its intention to allow the formation of private commercial banks in Somalia. This would break the monopoly position presently enjoyed by the Commercial and Savings Bank. Since that time, discussions have been held with several foreign and domestic interests but, to date no one has expressed interest in forming a new bank. As a result of a consultant's study, the managerial and accounting practice of the Commercial and Savings Bank are being reviewed. Late last year, the management of the bank was changed and it is foreseen that this may permit a quicker implementation of some of the study's recommendations.

Net domestic credit is expected to rise by about 8 percent in 1986, compared with 19.5 percent in 1985 and an objective for that year of 6 percent. The lower credit growth reflects an almost 6 percent decline in net credit to the Government and permits an expansion of credit to the rest of the economy of about 20 percent compared with an actual rise of 16 percent in 1985. The banking system's liabilities in Somali shillings to the private sector rose by only 8.3 percent in 1985 and are projected to rise by about 11 percent in 1986. However, the target growth for these liabilities will be heavily affected by the timing of purchases by the private sector under the commodity assistance programs. Total monetary liabilities, including foreign currency deposits and counterpart funds, are likely to grow by 10 percent, compared to 49 percent in 1985.

The targeted expansion in the money supply involves an increase in the velocity of circulation, compared with a reduction in 1985, when all deposit liabilities of the banking system are taken into account. The increase in velocity is expected to provide consistency with the program's objective of lowering inflationary pressures, while at the same time not generating undue pressure on the free market exchange rate. An additional benefit will be to provide incentives to Somalis to repatriate funds being held abroad.

As has been mentioned earlier, it is expected that there will be a significant increase in import duty collections in 1986. A large proportion of imports are made available by donors through commodity assistance programs. For administrative reasons, these imports do not become available early in the year, but are heavily concentrated in the latter part of a calendar year. Consequently, in the first few months of the year, it is expected that the availability of counterpart funds emerging from these programs will be at a low level and that the implementation of Somalia's investment program will require some utilization of net bank credit during this period. The program foresees that the Government will use So. Sh. 0.3 billion in net credit in the first two months of the year and a cumulative total of So. Sh. 0.4 billion through April, 1986 (Table 9). It is, however, expected that these resources will be repaid within the calendar year, and the target of overall net repayment to the banking system established in the budget will be met. The availability of credit to the rest of the economy is considered to be sufficient to allow the utilization of the commodity assistance and to encourage further improvements in private sector economic activity.

5. Public enterprises

The Government was supposed to accelerate the reorgarnization of the public sector in 1985 by classifying existing public sector enterprises into three categories: (1) those to be phased out of operations; (2) those to be privatized or converted into joint ventures; and (3) those to remain in the public sector. The Government has encountered

Table 9. Somalia: Quantitative Performance Criteria, 1984-86

(End of period)

	1984	1985				1986
	Dec.	March	June	Sept. 1/	Dec. 1/	April
		(In millions of Somali shillings)				
Net domestic credit 2/						
Ceiling		9,703.0	9,840.0	9,995.0	10,150.0	12,200.0
Actual	9,616.2	9,666.0	9,788.6	11,525.6	11,496.0	
Net credit to Government 2/						
Ceiling		4,415.0	4,448.0 3/	4,448.0	4,448.0	5,800.0
Actual	4,378.1	4,413.4	4,419.2	6,049.0	5,421.0	
		(In millions of U.S. dollars)				
External debt service payments arrears 4/						
Ceiling		...	--	--	--	38.6
Actual	146.9	30.2	22.7	34.3	46.6	

Sources: Central Bank of Somalia; and staff estimates.

1/ Indicative ceilings.

2/ Net domestic credit comprises credit to Government, public enterprises, and private sector less government deposits with the banking system. Net credit to Government comprises the banking system's claims on the Government, less government deposits, plus any budgetary use of local currency counterpart in respect of purchases from the Fund, plus losses accruing to the Central Bank from the operations of the dual exchange rate system.

3/ Ceiling adjustable downwards by any gap-fill resource in excess of So. Sh. 250 million.

4/ Excluding debt to Abu Dhabi, Saudi Arabia (other than Saudi Fund), and China frozen on the basis of verbal agreements. Excludes US$6 million in letters of credit for which there is uncertainty as to government guarantee.

difficulties in carrying out this plan due to a lack of proper accounting procedures in many enterprises and to a lack of consensus with regard to the elements which are to be used in the classification of enterprises. Importantly, very little interest has been demonstrated by the private sector in acquiring existing public enterprises, given the financial difficulties which many still face. Consequently, the Government has asked the World Bank for a mission to review the status of the public enterprise sector and to assist in the development of an appropriate strategy. Pending the results of this mission, the program does not contain any further commitments in this sector, because it does not want to prejudice the conclusions of this mission. However, the Government has indicated that it continues to give a high priority to an improvement in the sector.

6. Balance of payments prospects

Balance of payments developments in the medium term are likely to remain difficult for Somalia, because of the continued ban on cattle imports in traditional markets, the large projected debt service ratio, and continued problems with the timeliness of disbursements of foreign assistance. On the basis of present knowledge for 1986, the staff projects that private transfers and net capital inflows will fall slightly from the levels recorded in 1985. However, several large donors have yet to formulate their lending program for 1986, and it is likely that the actual receipts of resources will be larger than presently estimated. A further large increase in exports is projected on the basis of present livestock contracts, yet exports will still be below the 1982 level. It is expected that employment conditions in the neighboring oil exporting countries will continue to be difficult, and that private transfers will fall somewhat. On the basis of possible debt relief and additional capital flows, the staff foresees that the balance of payments financing gap can be closed. It should be noted, however, that of, the debt relief Somalia is requesting, some US$36 million out of the total US$108 million relates to previously rescheduled debt and moratorium interest. If Somalia cannot obtain relief on such exceptional terms, the resulting gap will need to be filled by donor support or by additional adjustments. During the review the staff will look into the progress made in filling the gap. Filling the gap will permit a 6 percent increase in imports denominated in U.S. dollars, the maintenance of gross reserves at a level of four weeks of cash imports, and a net repayment of arrears of US$18 million. Present projections allow for a 30 percent increase in cash imports financed through the free market, thus permitting a more than proportional improvement in import duty collection because these imports attract the highest duties (Table 10).

The present staff projections indicate that the balance of payments financing gap should disappear by 1990. This will require a growth of exports of about 15 percent per annum between 1986 and 1989, largely of livestock. It also assumes a gradually increasing inflow of official

Table 10. Somalia: Medium-Term Balance of Payments, 1984-91

(In millions of U.S. dollars)

	1984	1985	1986	1987	1988	1989	1990	1991
Current account	-145	-143	-169	-114	-106	-97	-78	-83
Exports, f.o.b.	62	107	130	153	167	185	203	224
Livestock	(33)	(77)	(95)	(113)	(123)	(135)	(147)	(161)
Bananas	(14)	(13)	(15)	(17)	(18)	(20)	(22)	(24)
Others	(15)	(17)	(20)	(23)	(26)	(30)	(34)	(39)
Imports, c.i.f.	-406	-400	-425	-451	-484	-521	-544	-595
Cash	(-156)	(-111)	(-142)	(-120)	(-130)	(-144)	(-144)	(-169)
Grants-in-kind	(-151)	(-127)	(-158)	(-194)	(-212)	(-232)	(-253)	(-276)
Loans-in-kind	(-99)	(-162)	(-125)	(-137)	(-142)	(-145)	(-147)	(-150)
Services (net)	-47	-51	-82	-60	-61	-63	-62	-63
Interest payments	(-44)	(-43)	(-79) 1/	(-60)	(-61)	(-63)	(-62)	(-63)
Other	(-3)	(-8)	(-3)	(--)	(--)	(--)	(--)	(--)
Transfers	246	201	208	244	272	302	325	351
Private	(72)	(33)	(30)	(50)	(60)	(70)	(72)	(75)
Official	(174)	(168)	(178)	(194)	(212)	(232)	(253)	(276)
Capital account	6	74	52	90	97	105	102	78
Official (net)	46	114	62	90	97	105	102	78
Inflows	(106)	(162)	(136)	(137)	(142)	(145)	(147)	(150)
Outflows	(-60)	(-48)	(-74)	(-47)	(-45)	(-40)	(-45)	(-72)
Private (net) 2/	-40	-40	-10	--	--	--	--	--
Overall balance	-139	-70	-117	-24	-9	8	24	-5
Financing	139	70	117	24	9	-8	-24	5
Central Bank	13	30	-11	-44	-55	-57	-24	5
Reserves	(9)	(-2)	(-4)	(-10)	(-13)	(-15)	(2)	(17)
IMF (net)	(-3)	(32)	(-5)	(-26)	(-34)	(-34)	(-19)	(-5)
Other	(7)	(--)	(-2)	(-8)	(-8)	(-8)	(-7)	(-7)
Commercial bank	29	-16	12	--	--	--	--	--
Arrears	71	-100	-18	-29	--	--	--	--
Gap/debt relief	26	156	134	97	64	49	--	--
Memorandum items:								
Gross reserves (in weeks of cash imports)	2	4	4	10	14	18	17	10
Current account deficit/GDP (in percent)								
Adjusted GDP 3/	11.9	11.0	11.8	7.3	6.2	5.2	3.9	3.7
Unadjusted GDP	3.8	5.1	8.4	...	...	...	...	...
Financing gap/quota (in percent)	...	...	303.2	218.4	144.2	111.8	--	--

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

1/ Includes payment of US$18 million in moratorium interest on 1985 debt relief.
2/ Includes valuation adjustment and net errors and omissions.
3/ GDP in Somali shillings converted at U.S. dollar rate necessary to maintain purchasing power parity at 1973 level.

transfers and capital, but at a considerably lower level than projected in EBS/85/1. Some revival in net private remittances is also foreseen, but they are not expected to reach the level recorded in 1984 until the end of the decade.

These trends will permit an increase in imports between 1986 and 1989 of about 7 percent per year in U.S. dollar terms. All of the outstanding external arrears should be paid off by 1987, and there is room for an improvement in the central bank reserves. Capital inflows are predicated on the indications provided by donors at the Consultative Group meeting and the support that they gave Somalia's public investment program. The medium-term balance of payments is financeable on the basis of this support and debt relief.

Without debt relief, debt service will total US$185 million in 1986, equivalent to a debt service ratio of 83 percent (Table 11). A similar level is estimated for 1987, although afterwards there will be a small reduction.

V. Staff Appraisal

The program launched by the Government of Somalia in 1985 and supported by a Fund stand-by arrangement involved ambitious measures to reorient the economy and reduce the large internal and external imbalances which plagued the economy. It aimed at stimulating private sector economic activity and at a major reduction of inflationary pressures. The program relied heavily on external assistance and received widespread donor support both at the Special Meeting organized by the World Bank and later at a meeting of the Paris Club. Most of the significant measures were implemented early in the year. In the external sector, the floating of the exchange rate for private transactions and the virtual elimination of trade restrictions and price controls was helpful in improving the allocation of resources and reaching the targeted level of exports. These exchange arrangements have functioned without official intervention and continue to be the cornerstone of government policy.

Foreign assistance fell below the targeted amount during the year and was heavily concentrated in the latter months of 1985. Consequently, substantial foreign exchange and import shortages surfaced in the early part of the year and for the year as a whole imports fell significantly below the targeted level. Consequently, the Government did not find it possible to repay its outstanding external arrears and indeed incurred additional ones, because of the substantial disequilibrium which appeared in the official foreign exchange market. The authorities took steps to minimize the gap by reducing their own outlays as much as possible, but, without the expected inflow of resources, they were unable to close the gap.

Table 11. Somalia: External Public Sector Debt Transactions, 1984-91 1/

	1984	1985	1986	1987	1988	1989	1990	1991
	(In millions of U.S. dollars)							
External debt	1,348	1,693	1,872	2,006	2,125	2,237	2,314	2,380
Non-IMF (excluding gap)	1,246	1,551	1,609	1,673	1,762	1,859	1,954	2,025
IMF	102	142	129	103	69	35	16	11
Financing gap (cumulative)	--	--	134	231	294	344	344	344
Debt service payments								
Principal payments	64	67	84	70	76	78	71	60
Non-IMF (exlcuding gap)	61	51	57	44	42	44	52	55
Disbursed end-1984	(61)	(51)	(57)	(44)	(42)	(44)	(45)	(43)
Projected	(--)	(--)	(--)	(--)	(--)	(--)	(7)	(12)
IMF	3	16	27	26	34	34	19	5
Interest payments	44	42	52	52	54	56	56	57
Non-IMF	39	29	35	31	30	32	33	35
Disbursed end-1984	(39)	(28)	(30)	(24)	(20)	(19)	(17)	(16)
Projected	(--)	(2)	(5)	(7)	(10)	(13)	(16)	(18)
IMF	5	13	13	11	8	5	2	1
Financing gap	--	--	4	11	16	19	21	21
Debt service (accrual basis) 2/	108	108	136	122	130	134	127	116
Arrears accumulation	97 3/	-67	-18	-29	--	--	--	--
1985 debt relief 4/	...	129	-33	-18	-18	-11	-6	-31
Principal	(...)	(27)	(-7)	(-11)	(-11)	(-4)	(--)	(-25)
Interest (net)	(...)	(19)	(-26)	(-7)	(-7)	(-7)	(-6)	(-6)
Arrears	(...)	(82)	(...)	(...)	(...)	(...)	(...)	(...)
Debt service (cash basis) 5/	11	47	187	170	148	145	133	147
Principal	4	30	102	99	87	82	71	84
Interest	7	17	84	71	61	63	62	63
	(In percent)							
Memorandum items:								
Debt service ratio								
Accrual basis	58.1	55.0	61.1	45.2	43.2	40.0	34.9	29.5
Cash basis	5.9	23.9	84.2	62.6	49.1	43.3	36.6	37.2
Interest payments ratio								
Accrual basis	23.7	21.0	23.2	19.3	18.0	16.8	15.4	14.4
Cash basis	3.8	8.5	38.1	26.1	20.3	18.7	17.2	15.8
IMF debt service ratio	4.3	14.7	18.0	13.5	14.1	11.7	5.9	1.6
Average interest rate	3.3	2.7	2.9	2.7	2.6	2.6	2.5	2.4
External debt/GDP	111.0	129.9	131.4	129.0	125.2	120.7	114.3	107.6

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

1/ Covers medium- and long-term disbursed debt only.
2/ Scheduled payments before arrears accumulation and 1985 debt relief.
3/ Includes debt relief of US$26 million.
4/ Debt relief on medium- and long-term debt; repayments include service on consolidated short-term debt.
5/ Actual payments, net of debt relief; also includes payment of arrears and amounts do not therefore directly correspond to balance of payments data.

While shortfalls in foreign assistance were an important factor in moving the program off course, the lack of progress in unifying the exchange markets and in implementing other policies in crucial areas such as the budget were also equally significant as contributory factors. Government purchases in the free market and the shifting of items out of the official market to achieve a more balanced position were limited. In addition, after the initial adjustments in the exchange rate which were carried out in the first half of 1985, the authorities did not make further adjustments in the second half, leading to a widening of the gap between the official and the free market rates. Progress in amalgamating the markets would have furthered the viability of the exchange system and reduced the amount of external arrears accumulated during the year. However, this would have also resulted in a larger depreciation of the exchange rate, which the authorities felt was unwarranted by real factors.

It is the intention of the authorities to unify the exchange markets by the end of 1986. The measures agreed in the current program are aimed at achieving this objective. If the formula included in the program is seen at the time of the review not to lead to the desired unification, significant adjustments would be made in the formula to facilitate the unification on time. The authorities are also aware that, notwithstanding the increase in the surrender requirement and the further depreciation of the official rate, a potential gap exists in the official market and that they would have to make purchases in the free market if arrears are to be avoided.

The adjustments in domestic petroleum prices are important in allowing pricing to reflect import costs and in permitting the shifting of petroleum imports into the free market. The authorities must move quickly in the attainment of their stated objective of reaching import parity in order to relieve pressure on the official market. The recently announced intention of allowing private sector imports of petroleum products should help in this regard.

Developments in the external sector will continue to be difficult for Somalia. There is still uncertainty as to the actual level of capital inflows and their timing during the year. Developments will require continuous monitoring and adjustment of policies as needed. In this regard it is important for donor governments to understand the important role their assistance plays in the orderly development of the external sector and in the attainment of the objectives of this program. Similarly, the authorities should not hesitate to adjust and tighten the program whenever there is a danger that the objectives of the program may not be met.

The outturn in the 1985 budget clearly demonstrates a slippage in fiscal policy. In part, it can be explained by a shortfall in the level of foreign assistance. However, at the same time, the revenue performance fell below target and there was some excess expenditures in the ordinary budget. The objectives of the 1986 budget will not be easy to attain and will require continued monitoring of events. The large increase in revenues projected for the year is possible but will require sustained improvements in the revenue administration, while it will be necessary to implement the current expenditure policy very strictly.

The overall budgetary deficit including grants at 4.5 percent of GDP (13.8 percent excluding grants) is at a high level and it is only acceptable in view of the expected grants and concessional loans which Somalia is likely to receive in 1986. If these resources fail to materialize, it will be necessary for the Government to take compensatory action in order not to permit the deficit to grow beyond the targeted level. In this regard, the target of a small reduction in the Government's position with the banking system is of critical importance, because it is the key to permit the private sector to receive needed financing resources, while at the same time attaining a lower inflation rate.

The staff is heartened by the authorities' intentions to implement the public investment program as agreed with the World Bank and hopes that donors will continue to support this intention by financing only projects which are included within the core program as was agreed at the Consultative Group Meeting for Somalia in November 1985.

The Government of Somalia should move quickly to finalize its outstanding bilateral agreements with respect to the 1985 Paris Club rescheduling. It is only then and on the strength of reasonable progress in implementing the adjustment program, that Somalia could hope to obtain appropriate support from creditors and donors.

The program proposed by the Somali authorities represents a comprehensive adjustment effort, but its implementation will not be an easy task for the authorities, as it is being carried out at a time in which the economy of Somalia remains weak and large scarcities of resources are evident. In addition, Somalia continues to face important administrative limitations and without the timely disbursements of agreed foreign assistance resources and implementation of the adjustment policies under the program shortages could easily emerge, which could threaten the attainment of some of the objectives. The authorities' strong commitment to take compensatory measures as required is an important element of the program. The Fund, together with the World Bank, will continue to play a role in mobilizing the necessary external financial support. The review of the program is expected to play an important role in reviewing the progress made and in making the necessary adjustments in policy to ascertain that the objectives of the program will continue to be met.

VI. Proposed Decisions

The following draft decisions are proposed for adoption by the Executive Board:

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/85/1, 1/2/85) and paragraph 35 of the letter attached thereto concerning deviations in the observance of the performance criteria in 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 policies and measures that the authorities will pursue during the period through September 30, 1986, and (c) to establish suitable performance criteria subject to which purchases may be resumed by Somalia.

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

3. Accordingly, 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

(a) during any period in which the data at the end of the preceding period indicate that

(i) the limit on total domestic credit of the banking system described in paragraph 17 of the letter of April 22, 1986, or

(ii) the limit on net credit from the banking system to the Government described in paragraph 17 of the letter of April 22, 1986, or

(iii) the target for the reduction of external payments arrears described in paragraph 12 of the letter of April 22, 1986,

is not observed; or

(b) after May 30, 1986, until the review of the arrangement regarding understandings on the balance of payments gap, exchange rate, and budgetary and petroleum pricing policies as contemplated in paragraph 20 of the letter of April 22, 1986 has been completed.

4. Paragraph 1 of the stand-by arrangement is amended by substituting "SDR 20.1 million" for "SDR 22.1 million".

5. Paragraph 2(a) of the stand-by arrangement on the phasing of purchases is amended to read:

"Purchases under this arrangement shall not, without the consent of the Fund, exceed the equivalent of SDR 2.0 million until April 23, 1986, the equivalent of SDR 11.66 million until May 31, 1986, and the equivalent of SDR 16.88 million until June 15, 1986."

6. 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 is completed; and that, notwithstanding the nonobservance of the performance criteria on payments arrears and multiple currency practices, Somalia may resume the making of purchases under the stand-by arrangement.

7. In accordance with Executive Board Decision No. 7908-(85/26) of February 20, 1985, on overdue payments to the Fund, the stand-by arrangment for Somalia is amended to read as set out in the attachment.

Exchange system

1. The exchange arrangements described in EBS/85/1 and EBS/86/93 give rise to restrictive multiple currency practices subject to approval under Article VIII, Sections 2(a) and 3.

2. The Fund notes the intention of the Government of Somalia to eliminate these multiple currency practices in the context of the adjustment program described in EBS/86/93, and grants approval of these practices through December 31, 1986.

Somalia - Stand-By Arrangement

Attached hereto is a letter dated November 8, 1984 from the Minister of Finance and the Governor of the Central Bank of Somalia, with attachments, requesting a stand-by arrangement and setting forth

a. the objectives and policies which the Government of Somalia intends to pursue for the period of this arrangement;

b. the policies and measures that the Government of Somalia intends to pursue through June 30, 1985; and

c. understandings of the Government of Somalia with the Fund regarding a review that will be made of progress in realizing the objectives of the program and of the policies and measures that the Government of Somalia will pursue for the remaining period of this arrangement.

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

1. For a period of twelve months from the effective date of this arrangement, Somalia will have the right to make purchases from the Fund in an amount equivalent to SDR 22.1 million, subject to paragraphs 2, 3, 4, 5, and 6 below, without futher review by the Fund.

2. a. Purchases under this arrangement shall not, without the consent of the Fund, exceed the equivalent of SDR 2.0 million until April 30, 1985, SDR 5.0 million until July 31, 1985, SDR 10.7 million until October 31, 1985 and SDR 16.4 million until January 31, 1986.

b. None of these limits shall apply to a purchase under the 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 borrowed resources beyond 12.5 percent of quota.

3. Purchases under this arrangement shall be made from ordinary resources and from borrowed resources in the ratio of 1 to 1, 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.

4. Somalia shall not make purchases under this arrangement that would increase the Fund's holdings of its 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:

(a) during any period through June 30, 1985 in which the data at the end of the preceding period indicate that:

(i) the limit on total net domestic credit of the banking system or the limit on net credit from the banking system to the Government, both specified in paragraph 21 of the attached letter; or

(ii) the limits on external payments arrears specified in paragraphs 11 and 14 of the attached letter,

is not observed; or

(b) during any period after June 30, 1985, until the review contemplated in paragraph 35 of the attached letter has been completed; or

(c) after June 30, 1985, until suitable performance criteria have been established in consultation with the Fund as contemplated by paragraphs 21 and 35 of the attached letter, or after such performance criteria have been established, while they are not being observed; or

(d) during the entire period of this stand-by arrangement, if the limit on contracting or guaranteeing nonconcessional external loans with a 1 to 12 year maturity or the limit on the accummulation of new short-term debt other than normal trade-related credits, described in paragraph 13 of the attached letter, is not observed; or

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

(i) imposes or intensifies restrictions on payments and transfers for current international transactions, or

(ii) introduces or modifies multiple currency practices other than the elimination of the dual exchange rate sytem, or

(iii) concludes bilateral payments agreements which are inconsistent with Article VIII, or

(iv) imposes or intensifies import restrictions for balance of payments reasons.

When Somalia is prevented from purchasing under the 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 stand-by 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 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 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 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 stand-by 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 repurchase 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 arrangement Somalia shall remain in close consultation with the Fund. These consultations, including those pursuant to the provisions of paragraph 35 of the attached letter, 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.

12. In accordance with paragraph 35 of the attached 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.

Mogadiscio, Somalia
April 22, 1986

Mr. J. de Larosière
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Mr. de Larosière:

1. Following mounting external and internal imbalances, the Government of Somalia embarked in early 1985 on a comprehensive economic and financial program aimed at stabilizing the economy, while raising the rate of economic growth. The program not only involved the implementation of far-reaching economic reforms to attain external viability over the medium term, but also a step-up in foreign assistance to help finance the expected balance of payments gap and repay outstanding payment arrears.

2. In the external sector, the program involved the liberalization of export and import restrictions and the introduction of a new exchange arrangement that ensured the determination of the exchange rate for most nongovernment transactions in accordance with market conditions. The reforms in the external sector were to be supported by a tightening of financial policies, a reform of the public enterprise sector, and the implementation of an expanded investment program.

3. The new exchange system was intended to lead to an increase in foreign exchange receipts by improving export profitability and by encouraging the inflow of remittances and to a rationing of import demand through the price mechanism. These additional resources, together with an expanded foreign assistance program and debt rescheduling, aimed at a small overall surplus and the virtual elimination of outstanding external payment arrears. The strengthening of the external sector through the eventual unification of the exchange markets was also foreseen.

4. The implementation of the program in 1985 suffered from some important shortcomings. There was a considerable delay in the release of the special gap-fill resources agreed by donors, and the level of foreign exchange receipts, largely from workers' remittances, has fallen short of expectations. The latter resulted from the more difficult employment conditions prevailing in the Gulf States. The lower availability of foreign exchange resources resulted in substantial shortfalls from the targeted level of imports and the emergence of new external payment arrears, including to the Fund. These arrears have, in turn, led to reduced drawings on loans from various international organizations and governments, compounding the balance of payments financing problems and causing a halt to many development projects.

5. Despite these difficulties, developments under the program have shown an important degree of success in various areas, and the Government of Somalia intends to strengthen the program in order to improve the success of the adjustment effort. Achieving this objective, however, will continue to be closely linked with the type, level, and timeliness of donor support. In this regard, the Government of Somalia is encouraged by the favorable outcome of the recent Consultative Group Meeting for Somalia chaired by the World Bank.

6. With the help of favorable weather conditions, the efforts made by the Somali Government to enhance agricultural production, including the new price and marketing policies, are having a positive impact on agricultural production. The increase in production is estimated to have resulted in an increase in real GDP of at least 4 percent, while the better supply conditions resulted in the rate of inflation for the year as a whole (December/December) declining to about 30 percent, compared to 82 percent in 1984. The pricing policies have had a particularly favorable impact on exports which are estimated to have increased by about 73 percent over the depressed 1984 level. Especially notable is the almost doubling of livestock exports, despite the continued ban of Somali cattle imports in a traditional market. The increase in exports was roughly in line with the projections included in the program, and consequently, the continued financing difficulties experienced in 1985 were largely the result of a lower inflow of remittances and of donor finance. Although there was a net decline in the outstanding stock of external arrears during 1985 as a result of rescheduling agreements, the Government is very concerned that new arrears were incurred as a result of these financing difficulties.

7. To date, only two bilateral agreements out of the four under the Paris Club accord of March 1985 have been concluded, but the Government is confident that the remaining ones will be finalized shortly. A request has been sent to the Secretariat of the Paris Club for the participating creditors to meet to discuss the provision of additional debt relief in 1986.

8. Although revenue collections have fallen considerably below the target established in the program for 1985, in part because imports fell 30 percent below the initial estimate, the government has made every effort to restrain expenditure, such that the overall deficit, (including grants) for 1985 is presently estimated at 3.9 percent of GDP, compared to a target under the stand-by arrangement of 2.0 percent. These developments have resulted in use of net domestic bank borrowing equivalent to 15.9 percent of the initial broad money stock. This outcome exceeded the target established in the program, which provided for no domestic financing, but, given the difficulties encountered, reflects considerable effort on the part of the government to meet the established objectives. Given the changed circumstances during the year, the Government feels this outcome reflects the strong government commitment to the program.

9. The delay in completing the scheduled review under the stand-by arrangement resulted in an interruption of Somalia's right to make the remaining purchases under the arrangement. Accordingly, in order to permit a resumption of purchases and continued implementation of the program, the Government of Somalia hereby requests a waiver of the performance criteria on external arrears set for March and June 1985, and an extension of the period of the current stand-by arrangement. Below, the government enumerates the economic and financial policies it will pursue during this period.

10. The government intends to unify the free and official foreign exchange markets in the course of 1986. To implement this policy, the official exchange rate was fixed at So. Sh. 54.5 = US$1 on January 21, 1986, was further depreciated to So. Sh. 58.5 on March 1, 1986, and will be depreciated by So. Sh. 4 per month for the rest of the year. During June, the Government of Somalia will review with the Fund this schedule to ascertain whether developments indicate a change in the amount of the depreciation so that by the end of 1986, the full unification can be achieved. The Commercial Bank will be adjusting its exchange rate to the weighted average of the private market rate of the previous 10-day period every 1st, 11th, and 21st day of each month. At the same time, the base for the calculation of import duties will be adjusted to the posted rate declared by the Commercial Bank, as detailed above, providing increased restraint on import demand and additional revenue for the budget. The minimum export prices for livestock will also be increased in March 1986 to reflect current market conditions more accurately.

11. Since June 1985, domestic petroleum prices have been adjusted several times with the aim of reaching import parity. In the pursuit of this objective, the Government has been adding So. Sh. 2 per liter and So. Sh. 1 per liter to gasoline and diesel prices respectively on the first day of each month, beginning in February. The government is prepared to speed up this schedule if it will not reach import parity for gasoline by April 1986 and for diesel by June 1986. With the liberalization of the economy, the private sector has been given authorization to import and distribute petroleum products. The new pricing policy will facilitate this objective.

12. The current exchange system is providing considerable incentives for exports. These are projected to increase by about 22 percent in 1986. Remittances from Somali workers abroad are also significant when consideration is given to the difficult labor conditions in the Gulf States. Thus, in the short term, it is not feasible to foresee increases in export earnings of the magnitude necessary to close the projected balance of payments gap for 1986. At the same time, the reduction in imports which has occurred since 1981 has meant that further significant reductions in import volumes are likely to have a very negative impact on

economic activity. Consequently, for the next few years Somalia must rely on special donor assistance, to be raised through the Consultative Group process of the World Bank, and by further rescheduling of debts. For 1986, it is foreseen that the balance of payments will have a financing gap of about US$135 million, of which US$108 million represents debt service payments in respect of which Somalia has requested, or intends to request, a rescheduling. While a favorable response has been received for donor financing of the 1986 balance of payments, as in 1985, there are delays being encountered in arranging for these resources and in obtaining the necessary amount in the form of cash and/or petroleum products, but the Government is confident the additional resources will emerge. These difficulties will mean that Somalia will only be able to reduce the outstanding stock of payment arrears, which are estimated at US$47 million at end-1985, by US$9 million in the first half of the year, and by US$18 million for the year as a whole. However, to the extent that cash resources permit, the Government will aim for a larger reduction of external arrears over the year as a whole. On January 1, 1986, Somalia informed the Paris Club creditors that they were requesting a rescheduling of payments falling due in 1986. Net external arrears will be reduced by at least US$8 million by end-April 1986 from the end-December 1985 level. These amounts exclude overdue payments for which Somalia is seeking a rescheduling. It must be noted that, at the recent Consultative Group Meeting for Somalia, the World Bank recommended to bilateral and regional participants to whom these obligations are owed, but who cannot reschedule, to find alternative ways of providing net resources to Somalia to permit the clearing of these arrears.

13. The economy is expected to continue to expand by at least 4 percent in 1986, with a higher growth rate projected for the medium term. Moreover, a further major reduction in inflationary pressures is projected, with the cost-of-living index estimated to rise by about 22 percent.

14. The 1986 budget has recently been revised in the light of the envisaged exchange rate policy. It provides for an overall deficit (including grants) of 4.5 percent of GDP including the net impact of the new exchange rate policy compared to 3.9 percent in 1985. Excluding grants, the deficit will rise from 9.8 percent of GDP in 1985 to 13.8 percent in 1986. However, the government's net domestic indebtedness will decline as result of the expected rescheduling. The budget includes a 60 percent increase in revenue collections. The higher yield is expected to come from the changing of specific tax rates to ad valorem basis and the broadening of the coverage of excise duties already in place, the higher import duty base previously mentioned, and administrative improvements, which are being implemented. In August 1985, a new Ministry of Revenue was created. As a result, in the fourth quarter revenue yields increased significantly, compared with the third quarter. The attainment of the revenue objective, however, will require continuous monitoring and additional measures, if necessary. At the same time, total expenditures are

expected to double in 1986, in part reflecting the exchange rate action. Ordinary outlays are estimated to rise by 20 percent. The budget provides for a more than doubling of investment outlays, reflecting available project and commodity assistance in light of the new exchange rate policy and an increase in implementation capabilities. These levels of outlays have been agreed with the World Bank in their review of the investment program. Investment outlays will rise from about 6 percent of GDP in 1985 to 12 percent in 1986. Most of these outlays will be foreign financed. Consequently, shortfalls in implementation should not affect the domestic financing requirement. The government intends to maintain an unchanged wage bill during the year and proceed with the reform of the civil service.

15. Given the recommendations made by the World Bank to the recent Consultative Group Meeting on Somalia's public investment program, it is foreseen that the level of grants will remain at least at the present level for a number of years, particularly as emphasis is being given to shifting assistance from loans to grants. Thus, project and commodity assistance is expected to remain at the present level for a number of years. Difficulties will emerge, however, in the event that assistance in cash form and in petroleum falls short of the recommendations made by the World Bank.

16. In line with the liberalization of the domestic economy, the government plans to continue with the reform of the public enterprise system. For this purpose, the Somali Government, together with the World Bank will review possible strategies during a mission to take place in the second quarter of 1986. As a result of this mission, the authorities intend to develop a strategy for speeding up the reform of public enterprises.

17. For 1986, net domestic credit is projected to expand by 8 percent, compared to an estimated expansion of 20 percent in 1985. Such an expansion is below the projected growth in nominal income and should lead to a deceleration of the growth of broad money. As none of the credit will be utilized by the central government budget (except for seasonal purposes), all of available credit will be directed towards the rest of the economy. Consistent with these targets, net domestic credit, which was So. Sh. 12.5 billion at the end of October 1985 and is estimated at So. Sh. 11.5 billion on December 31, 1985, will not be allowed to exceed So. Sh. 12.0 billion on April 30, 1986. Net credit to the government, which was So. Sh. 6.5 billion in October 1985 and is estimated at So. Sh. 5.4 billion in December 1985, will not exceed So. Sh. 5.8 billion on April 30, 1986.

18. In February, the government increased the maximum interest rate on commercial bank deposits by 4 percentage points to 22 percent. As a consequence, the maximum deposit rate will be in line with the projected rise in consumer prices for 1986.

19. In view of the already high debt service ratio, the government will refrain from contracting or guaranteeing any nonconcessional external loans with a 1 to 12-year maturity or any short-term credits, other than normal trade related credits, during 1986, except and up to US$24 million of short-term borrowing which may be necessary to make payments to the Fund. Amounts of debt rescheduled are excluded from these limits.

20. The Government of Somalia intends to reach understandings with the Fund prior to the end of June on the financing of the balance of payments gap, the exchange rate, budgetary policies, petroleum pricing, and on the performance criteria for the rest of the program. The Government of Somalia feels that the measures outlined in this letter are sufficient for meeting the objectives of policies established for 1986. It will take any additional measures that may become necessary for this purpose.

Sincerely yours,

Dr. Mohamed Sheikh Osman
Minister of Finance

Dr. Omar Ahmed Omar
Governor
Central Bank of Somalia

SOMALIA - Relations with the Fund
(As of March 31, 1986)

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:	172.7 (390.6 percent of quota)
(c) Fund credit:	128.5 (290.6 percent of quota)
Of which: Credit tranches	25.4 (57.5 percent of quota)
Enlarged access	70.5 (159.4 percent of quota)
Compensatory financing facility	32.6 (73.8 percent of quota)

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

(a) Current stand-by:

(i) Original duration from February 22, 1985 to February 21, 1986 extended to June 30, 1986	
(ii) Amount:	22.1
(iii) Utilization:	2.0
(iv) Undrawn balance:	20.1

(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:	--

SOMALIA - Relations with the Fund (continued)

(i)	Duration from February 27, 1980 to 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:	0.0 (0.0 percent of net cumulative allocations)

V. Administered Accounts

(a) Trust Fund loans

(i)	Disbursed:	10.7
(ii)	Outstanding:	10.7

(b) SFF Subsidy Account — None

VI. Overdue Obligations to the Fund: --

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 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

SOMALIA - Relations with the Fund (concluded)

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 = U.S.$1 from June 5-December 31. On January 1, 1986, the official rate was devalued by So.Sh. 1.8917 per U.S.$, bringing it in line with the earlier agreement to devalue by 0.5 So. Sh. per U.S.$ per month. On January 21, the official rate was devalued by So. Sh. 12 per U.S. dollar, and on March 1, and April 1, the rate was further devalued in accordance with agreements reached in November and January to devalue the rate by So.Sh. 4 per month. At April 1, the official rate was So. Sh. 62.5 per U.S. dollar, the posted rate at the commercial bank was So. Sh. 83.6133 per U.S. dollar, and the market rate was about So.Sh. 150 per U.S. dollar.

IX. Last Article IV consultation and stand-by review:

The last Article IV consultation discussions were held in Mogadiscio during April 24-May 9, 1985; the Executive Board discussed the staff report (SM/85/203 and SM/85/215) on August 9, 1985. Discussions for the review under the current stand-by arrangement were held in Mogadiscio during June 27-July 4, 1985 and continued during the September 5-15, 1985 and November 1-4, 1985 staff visits to Mogadiscio and Paris, respectively, the January 5-12, 1986 mission to Mogadiscio, and the March 6-9 staff visit to Mogadiscio.

X. Technical assistance:

(a) FAD: Since December 1983 an advisor from the FAD panel has been assisting the Ministry of Finance as a revenue advisor.

(b) CBD: Since October 1984 a consultant on external debt has been assisting the Ministry of Finance. The Central Bank is being assisted by a research advisor since August 1985 and a training advisor since December 1985.

(c) Other: A Bureau of Statistics mission reviewed in May 1985 the coverage, sectorization, and classification of monetary accounts.

XI. Resident Representative/ Advisor: Mr. Salvatore Schiavo-Campo assumed his post as resident representative to Somalia on March 27, 1985.