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Supplement 1

CONFIDENTIAL

August 12, 1986

To: Members of the Executive Board

From: The Acting Secretary

Subject: Burundi - Structural Adjustment Arrangement

Attached for the records of the Executive Directors is the text of the structural adjustment arrangement for Burundi agreed at Executive Board Meeting 86/134, August 8, 1986.

Att: (1)

Structural Adjustment Facility:
Three-year and First Annual Arrangements

Attached hereto is a letter with an annexed Policy Framework Paper and an annexed Memorandum of Economic and Financial Policies dated July 21, 1986 from the Minister of Finance of Burundi, requesting from the Fund a three-year structural adjustment arrangement and the first annual arrangement thereunder, and setting forth

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

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

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

1. For a period of three years from August 8, 1986 Burundi will have the right to obtain three successive loans from the Fund under the Structural Adjustment Facility in a total amount equivalent to SDR 20.069 million.

2. The first loan, in an amount equivalent to SDR 8.54 million, is available for disbursement at the request of Burundi.

3. The second and third loans will be available upon approval by the Fund of the corresponding annual arrangements and will be disbursed at the request of Burundi. The amount of the second loan will be equivalent to SDR 5.7645 million, and the amount of the third loan will be equivalent to SDR 5.7645 million.

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

(a) the indicators described in paragraphs 4 and 5 of the Memorandum of Economic and Financial Policies and specified in Tables 1 and 4 attached to that Memorandum,

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

(c) introduction or modification of multiple currency practices,

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

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

5. In accordance with paragraph 3 of the attached letter, Burundi will provide the Fund with such information as the Fund requests in connection with the progress of Burundi in implementing the policies and reaching the objectives supported by the first annual arrangement.

6. In accordance with paragraph 4 of the attached letter, Burundi will consult with the Managing Director on the adoption of any measures that may be appropriate at the initiative of the Government or whenever the Managing Director requests consultation because he considers that consultation on the program is desirable. These consultations may include correspondence and visits of officials of the Fund to Burundi or of representatives of Burundi to the Fund.

Burundi - Letter of Transmittal, Request for Three-Year Arrangement and the First Annual Arrangement Thereunder

Mr. Jacques de Larosière
Managing Director
International Monetary Fund
700 - 19th Street, N.W.
Washington, D.C. 20431

July 21, 1986

Dear Managing Director:

1. The annexed Policy Framework Paper has been prepared in collaboration with the staffs of the Fund and the World Bank. It describes the major economic problems and challenges facing Burundi, the objectives of a three-year medium-term program; the priorities and the broad thrust of macroeconomic and structural adjustment policies; and the likely external financing requirements, together with the available sources of such financing.

The Government of Burundi will remain in close contact with the staffs of the Fund and the World Bank on developments and progress in implementing these policies, and the Policy Framework Paper will be updated (annually) as the program is implemented.

2. The annexed Memorandum of Economic and Financial Policies pursuant to the policy framework described above sets out the objectives and policies that the Government of Burundi intends to pursue for the period July 1, 1986 to June 30, 1989, and the objectives and policies for the first year of this period, for which balance of payments assistance is needed. In support of these objectives and policies, Burundi hereby requests from the Fund a three-year structural adjustment arrangement in the amount that will be available to Burundi under the Fund's Structural Adjustment Facility, and the first annual arrangement thereunder.

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

4. The Government believes that the policies set forth in the attached Memorandum of Economic and Financial Policies are adequate to achieve the objectives of its program but will take any further measures that may become appropriate for this purpose. Burundi will consult with the Managing Director on the adoption of any measures that may be appropriate, at the initiative of the Government of Burundi or whenever the Managing Director requests such consultation.

Sincerely yours,

/s/ Pierre Ngenzi
Minister of Finance

Annexes: (1) Policy Framework Paper
(2) Memorandum of Economic and Financial Policies

BURUNDI

Medium-Term Economic and Financial Policy Framework (July 1, 1986-June 30, 1989)

I. Introduction

1. Burundi is a landlocked country with a high population density, limited natural resources, and low per capita income (US$240 in 1984). Social indicators compare with those of the poorest African countries. Population growth (2.9 percent per annum projected for the 1980-2000 period) is high. Agriculture is the mainstay of the economy, accounting for about 60 percent of GDP. Coffee is the principal export item (80-85 percent of total merchandise exports). The country has been able to maintain its self-sufficiency in food (at least for the most popular staples), and, despite the high demographic pressures on already constrained land, urban migration has been limited. At the same time, inadequate incentives and market distortions have hindered the diversification of production and exports. As a result, the economy is highly vulnerable to fluctuations in weather conditions and world commodity prices. Owing to its landlocked situation, Burundi often experiences serious domestic shortages and shortfalls in export revenues, especially when there are disruptions in the transportation conditions through neighboring countries. Moreover, the country lacks managerial skills and human capital--adult literacy is about 30 percent.

2. From 1978 to 1981, with increases in coffee export prices and public savings, and continued foreign assistance, there was an expansion of public investment. During this period, real GDP growth at factor cost averaged 5.2 percent a year, manufacturing value added grew at about 14 percent per annum, and investment as a percentage of GDP rose to 14 percent, compared with 8 percent in earlier years. Education coverage and basic infrastructure in roads and energy were expanded. However, developments on other fronts were not as satisfactory. The industrial growth was oriented mainly to the domestic market, and a protectionist system favored the creation of inefficient enterprises, including public enterprises which became heavily dependent on government support. Import growth associated with a rapid increase in domestic consumption and investment outpaced the growth of export earnings, which remained narrowly based on coffee. The current account deficit of the balance of payments rose rapidly and so did the deficit in the central government operations. Administrative controls were put in place in areas of economic management, leading to economic distortions.

3. From 1982 to 1985 the economy of Burundi experienced slow and unstable growth rates in real GDP along with large domestic and external financial imbalances. During this period, domestic savings have been low (averaging about 4 percent of GDP) and have financed only a small

part of investment, which averaged about 17 percent of GDP. The overall deficits in central government operations (on a commitment basis) averaged about 9.1 percent of GDP, and were accompanied by heavy reliance on foreign borrowing, a growing indebtedness to the domestic banking system, and an accumulation of domestic arrears. Even though most development projects were largely aid-financed, the local currency outlays associated with both these projects and other government expenditures could not be covered by domestically generated revenues. In the external accounts, export earnings covered less than one half of the import bill. The deficit in the external current account (about 8 percent of GDP) entailed heavy foreign borrowing and contributed to a sharp rise in foreign debt service payments, to recurrent deficits in the balance of payments, and to a marked weakening in the country's net official reserve position. The latter fell from 3.8 months of imports in 1981 to 1.1 months of imports at end-1985.

4. In 1986 Burundi will benefit significantly from both a steep rise in coffee export prices and a sharp drop in petroleum import prices. These (albeit temporary) external factors provide an unusually favorable environment in which to start a program of structural adjustment. Recognizing this, as well as the urgent need to lay the foundations for higher rates of real economic growth and for medium-term balance of payments viability, the Government of Burundi has decided to implement comprehensive adjustment policies over a period of three years starting July 1, 1986.

II. Major Structural and Financial Problems

5. In recent years, several impediments to efficient resource allocation, real economic growth, and financial stability have become evident. These impediments are in the major policy areas relating to exchange rate policy, the system of import and exchange controls, the structure of effective tariff protection, the incentives for production of tradeable goods, the public investment program, the management of parastatals, and fiscal and domestic credit policies.

6. Following a noticeable real depreciation in the first quarter of 1984, the real effective exchange rate of the Burundi franc has appreciated significantly since then in relation to the base period 1980. This trend has made it difficult to provide the necessary price incentives for export production and has led to an import bias in the structure of production costs and of consumption.

7. In response to a declining trend in international reserves, since 1983 stricter selective controls have been applied to imports other than foreign aid financed imports. All imports (requiring release of foreign exchange) have been subject to tighter licensing regulations, and about 50 products have been subject to quantitative restrictions and/or prohibited. These developments have led to high levels of implicit protection for selected import-substitution activities, and have also,

to some extent, impeded the activities of those who might be hurt by such restrictions, including enterprises in the modern and the industrial sectors, which operate presently at low levels of capacity utilization. Since 1983 exchange restrictions have also been intensified for external transfers of earned income by foreign nationals; this has discouraged private foreign investments. The combination of trade and exchange restrictions as a whole has tended to encourage the emergence of an unofficial parallel exchange market.

8. The present structure of import tariffs is characterized by widely varying levels of tariffs within and across various sectors of the economy. Moreover, when the tariff equivalent of quantitative import restrictions is taken into account, the average level of effective protection is in many cases excessively high. Consequently, the structure of effective protection is not transparent to potential beneficiaries, as well as as to those who might be hurt by it, and is an impediment to efficient resource allocation.

9. During the first half of the 1980s, the performance of the parastatal sector has been disappointing, with several enterprises incurring losses, operating at a low capacity, and unable to carry out their own investment program or to service their foreign debt. These problems are the result of (a) poor management, (b) inadequate price policies, (c) deficient design, and (d) unclear relations with relevant ministries.

10. In the predominantly important agricultural sector, the prospects of maintaining self-sufficiency in food crops are limited because increasing demographic pressure is leading to an abandoning of the practice of fallow, cultivation of marginal lands, reduction in average farm size, and declining soil fertility. A higher level of productivity needs to be achieved through increased research, improved extension services, and rationalization of the sector's institutional organization. As regards export crops, there is a need to provide adequate incentives to producers, increase efficiency in resource utilization, and improve crop quality and marketing.

11. The implementation of public investment under the ongoing Fourth Development Plan (1983-87) has, up to the end of 1985, been slower than initially planned, due to financial constraints. It is also clear that if Burundi were to try to reach the initially planned target for public investment, it would entail excessively high annual levels of budgetary capital expenditure, and sizable overall deficits in central government operations. Such a development would not be compatible with cautious and prudent financial policies, and the desired progress toward medium-term balance of payments viability and a manageable foreign debt situation. The public investment program for 1986-88 needs to focus on economically viable and productive projects, to ensure a better balance between recurrent and capital expenditures, and to take into account the constraints of domestically generated budgetary revenues and of the likely availability of concessional foreign resources.

12. Over the past five years, the Central Government's financial operations have resulted in large deficits. On the revenue side, the main problems have been the substantial exemptions granted for import taxes, deficiencies in the current import tariff structure, weaknesses in the structure of the domestic transaction taxes, the reliance on specific rates rather than ad valorem rates for certain indirect taxes, a relatively heavy dependence on coffee export taxes, and inadequacies in tax administration and tax collection procedures. On the expenditure side, the expansion in past years has resulted mainly from increases in capital outlays and interest payments, and, more lately, also from a rise in the wage bill. During the early 1980s, with the rapid growth of expenditures in the face of a slow pace of revenue expansion, the process of budgetary control of expenditures weakened, leading to the accumulation of substantial domestic arrears. The financing of central government operations entailed a rapid buildup of the foreign debt as well as sizable recourse to domestic bank credit. These developments in turn have led to a sharp rise in the debt service burden and to rates of domestic credit and monetary expansion that were in excess of GDP growth.

13. Finally, during the past five years, a predominantly large share of domestic credit expansion has been absorbed by the Government, and the flows of bank credit to other sectors have been limited and uneven. Furthermore, domestic interest rates have been negative in real terms, and have thus not provided any incentives for financial savings and efficient resource allocation.

III. Overview of the Program

14. The structural adjustment program that Burundi will be implementing during the period from July 1, 1986 to June 30, 1989 will aim at a more rapid growth and diversification of the productive base of the economy, and at a reduction in external financial imbalances to levels that are consistent with medium-term balance of payments viability and the avoidance of excessive inflationary pressures.

15. Specifically, the medium-term objectives are (a) to generate a real GDP growth rate of about 4 percent a year (compared with a population growth rate of 2.9 percent), mainly through better performance in agricultural production and further expansion in manufacturing activities, (b) to reduce the annual domestic inflation rate from about 10 percent in 1986 to around 7 percent by 1989, and (c) to achieve an improvement in the balance of payments that is consistent with both a reduction in the country's external debt service ratio to about 18.5 percent of exports by 1989 and an increase in the net official foreign assets to the equivalent of at least three months of imports beginning end-1986. To achieve the latter, as a proportion of GDP the external current account deficit will have to be contained to 3.4 percent in 1986, 6.5 percent in 1987, and 7.0 percent in 1988-89. These objectives reflect annual real growth rates of 4 percent for

imports and 5 percent for exports; moreover, exports are to be diversified to reduce excessive dependence on coffee. Concurrently, the objectives for central government operations will be to limit the ratio of the overall deficit (on a commitment basis) to GDP to 0.3 percent in 1986, 2.4 percent in 1987, and in later years, to a level that is compatible with prudent financial management. With these objectives, the domestic savings ratio is to be raised from 4 percent during 1982-85 to about 7-8 percent during 1986-89, which would allow an investment/GDP ratio of about 16-19 percent during the program period.

16. To achieve these broad objectives over the next three years, major policy reforms will be implemented. These policy reforms will include (a) flexible exchange rate management and appropriate trade and industrial policy changes to expand and diversify exports; (b) measures to improve the quality of public development expenditures and efficiency of public enterprises; (c) improved incentives for agricultural production and exports; (d) measures to increase domestic resource mobilization in the public sector; and (e) financial sector policy reforms designed to ensure adequate growth in private savings and investment. A more detailed description of the policies to be pursued and of the foreign aid requirements during the program period are contained in the following sections.

A. External sector policies

17. In a major shift away from past policies, during the program period, the Government will be implementing a flexible exchange rate policy, a comprehensive reform of the trade regime, including a progressive liberalization of foreign trade and exchange controls, and a reform of the structure of tariff protection.

18. The main elements of exchange rate policy include early steps to correct the real effective appreciation that has occurred over the past few years; the adoption of a flexible mechanism for avoiding any new real effective appreciation; and the establishment of a set of specific criteria to be used as a guide for periodic adjustments in the exchange rate of the Burundi franc. With regard to the last element, the criteria that will be taken into account are (i) developments in the external current account, the balance of payments, and net official foreign assets in relation to the program's objectives; (ii) progress made in liberalizing the restrictions on external trade and payments; (iii) the implications of the reform of the tariff protection system; and (iv) trends in the real effective exchange rate. In addition to the periodic adjustments based on the above criteria, the Government will implement additional timely adjustments in the exchange rate of sufficient magnitude if this becomes necessary to achieve a structural improvement in the balance of payments over the medium term; such an improvement should be achieved through a more efficient use of factors of production (including labor) and an increase in competitiveness in tradeable goods and services.

19. The Government will undertake significant measures to liberalize foreign trade and exchange restrictions. Quantitative import

restrictions will be removed for all but a few luxury consumer products and three categories of imports competing with locally manufactured goods (textiles, glass, and pharmaceutical products). Import licenses will be granted automatically. The remaining restrictions on imports of luxury goods will be removed by end-1986. At that time, the restrictions on the three categories of imports competing with local production would be reviewed with a view to adopting a timetable for their elimination by end-1987 and their eventual replacement by appropriate tariffs. The decree regulating the import trade profession (No. 10017) has been amended in order to increase competition among importers. In addition, the existing limits applicable to foreign nationals for transfers of earned and rental incomes, profits, and dividends will be raised progressively.

20. A comprehensive reform of the (protective) import tariff structure will also be implemented in a phased manner, according to a precise timetable. The broad objectives of the tariff reform include both a progressive reduction in the (presently) high levels of effective tariff protection and the establishment of a narrower band of tariff rates (within, as well as across, various sectors).

21. Along with policies designed to contain the external current account deficit to a sustainable level, the Government will be taking steps to strengthen the management and the monitoring of the foreign debt. It intends to avoid any recourse to nonconcessional foreign loans. All new foreign borrowing contracted and/or guaranteed by the Government and the public entities will be limited to concessional loans. A committee comprising representatives from the Ministry of Finance, the ministry at the President's office in charge of planning, and the Bank of the Republic of Burundi will be responsible for managing and monitoring all external debt.

B. Policies affecting efficiency of resource allocation, and management of public expenditures and public enterprises

22. The Government has prepared a priority public investment program for 1986-88, which is consistent with the likely inflows of concessionary foreign aid and the projected availability of domestically generated budgetary revenues. This program puts an adequate emphasis on the development of agriculture (35 percent of total investment). The investment program has been jointly reviewed by the Government and the World Bank, and its economic justification was found to be, on the whole, adequate. Concerning the SOSUMO project, the Government is committed (as in the case of other public enterprises) to not subsidize the operating costs of the enterprise and to treat the sugar processing unit in the same way as the other infant industries with respect to tariff protection. The Government will use an international company with relevant expertise to manage the SOSUMO project. For all the components of the project (including the distillery), for which no contracts have yet been signed, the Government will conduct feasibility studies to assess their economic viability.

23. The public investment program will be implemented in annual tranches, which will be formulated on the basis of updated annual estimates of concessional resource inflows and of the budgetary local currency contribution that is compatible with the agreed fiscal objectives (discussed later). On this basis, the public investment target to be implemented by the Government has been set at FBu 19.1 billion for 1986, and preliminarily at FBu 22.7 billion for 1987. The budgetary local currency funds to be set aside for these investment targets will be FBu 3.0 billion for 1986 and FBu 3.1 billion for 1987; the remainder is expected to be covered by foreign grants and concessional loans. The public investment targets for 1987 and 1988 will be reviewed with the World Bank in due course to ensure an adequate balance between capital and recurrent expenditures and an appropriately restrictive stance of fiscal and credit policies.

24. For the public enterprise sector (including noncommercial enterprises) the Government's main objectives are (a) to ensure that government participation will be limited to those enterprises which require public investment either because they are vital public services (for example, water and electricity services), or because strategic sectors are involved (for example, petroleum exploration), or because certain activities may not be undertaken wholly by private investors alone; and (b) to maximize the contribution of viable public enterprises to GDP by ensuring that they operate efficiently. The main elements of the government strategy to achieve these objectives include (a) the rehabilitation of public enterprises whose medium-term economic profitability has been demonstrated; (b) improvements in public enterprise management; (c) the restructuring of the parastatal sector through privatization or cessation of activity when operations are not profitable over the medium run; and, as already decided by the Government, (d) the creation of an office in charge of the public enterprise sector with responsibility for coordinating the rehabilitation program of the sector as well as for monitoring developments.

25. Prices will be deregulated and public enterprises will be subject to the same market environment as the private sector. Exceptions would be made for those enterprises carrying out noncommercial social activities (which the Government may have to subsidize) and public utility monopolies for which price regulation will be appropriate, and would take into account the requirements of sound financial management.

26. In the context of the first IDA structural adjustment credit, the Government's action plan includes (a) the closure of four enterprises facing serious financial problems; (b) the reintegration in the public administration of one public enterprise performing noncommercial activities; (c) the rehabilitation of five other enterprises; and (d) assistance to six major enterprises to improve their economic performance in the medium to long term. The proposed IDA Fourth

Technical Assistance Project will provide support to this government action plan.

27. In agriculture, the Government will continue to let food crop prices be market determined, and will establish producer prices for export crops at levels sufficient to provide incentives for increased production and quality, taking into account the evolution of international prices. For the 1986/87 campaign, the Government has increased coffee prices by 28 percent, and tea prices by 20 percent, thus raising their prices in real terms. For the following years, prices will be determined on the basis of (a) the rural consumer price index; (b) exchange rate adjustments; and (c) prospects in domestic and foreign markets. The Government will also prepare a medium- and long-term strategy for the coffee sector, so as to define the policies required to increase production and quality and hence maximize export revenues, while maintaining an appropriate balance between export and food crop production.

28. The Government recognizes that a price control system in place for imported goods and for domestic manufactures and services is not consistent with the new trade liberalization policy and could hamper the process of relative price adjustment and of improved resource allocation that should occur with the tariff reform. It has, therefore, decided to liberalize prices at the same pace as imports. No control will be exercised on products for which importation is liberalized, and only in case of acute shortages, certain products, such as flour, sugar, paper, iron sheets, and powdered milk, would be submitted to a price ceiling. The price of petroleum products and cement will be controlled by the Government and adjusted periodically, taking into account the prices in international markets and fiscal considerations.

29. To improve the existing provisions of the Investment Code, the Government has decided to revise it in order to (i) not block the establishment of any new profitable activity, even if it competes with existing ones; (ii) eliminate the exemption of import duties on equipment and industrial imports, except for regional development projects and for projects with long gestation periods (four years or more); (iii) grant the benefits of the Investment Code to projects which have an economic rate of return of more than 10 percent and an investment cost per job of less than US$20,000; (iv) facilitate access of small enterprises to the benefits of the Code; and (v) reduce the review process for beneficiaries to a maximum of three months.

C. Fiscal policies

30. In an effort to achieve the medium-term fiscal objectives, the Government will be taking measures to improve the tax system, to restrain overall expenditure growth and ensure an appropriate balance between capital and recurrent outlays, and to limit the Government's recourse to bank financing to a level that is consistent with an adequate measure of restraint in domestic credit and monetary expansion.

31. The improvements to be implemented in the tax system will include the following: (i) the elimination of all noncoffee export taxes, to be followed by a progressive reduction in the coffee export tax; (ii) the replacement of the current turnover tax system by a single-stage sales tax collected on the domestic production of goods and services and on imports; (iii) a conversion of the specific base of consumption taxes to an ad valorem base; (iv) the progressive replacement of quantitative import restrictions by appropriate tariffs, and a comprehensive reform of the structure of the import tariff; (v) the reduction of import tax exemptions; and (vi) the strengthening of the auditing system and data base for taxpayers to ensure an improvement in tax collections.

32. In the coming years, the Government will make every effort to restrain the expansion of total expenditures and net lending to avoid an unsustainable increase in the overall deficit in central government operations. To limit expenditure growth, several measures will be taken. Cumulative quarterly ceilings will be established for all current expenditure commitments, to prevent both overspending against appropriations and the emergence of arrears. Public enterprises of a commercial nature will not be granted budgetary transfers and subsidies, and, in general, all public enterprises would be required to assume responsibility for their own debt service. Budgetary commitments for investment outlays will be limited strictly to actual disbursements of foreign grants and concessional loans and to the budgetary allocation of domestically generated tax revenues. Finally, the structure of the annual levels of public expenditure will be designed to give due weight to the need for adequate appropriations for maintenance outlays and to the need to restrain the wage bill and new investments to levels that are consistent with an adequately restrictive stance of fiscal policy.

D. Credit and interest rate policies

33. To contain pressures on the price level and the balance of payments, the Government is determined to follow a cautious monetary policy. Consistent with this broad objective, the annual growth rate of broad money will be limited to about 8 percent, and the Government will be taking appropriate steps to achieve the necessary degree of restraint in overall domestic credit expansion. In particular, to allow the private sector to finance its productive activities with an adequate flow of domestic bank credit, the Government will be reducing its net indebtedness to the banking system during 1986 and 1987 (by FBu 5.67 billion and FBu 5.91 billion, respectively). In 1988 and 1989, the Government will continue to maintain a cautious stance of credit and monetary policies.

34. In addition to adequate restraints on overall credit and monetary expansion, the Government will follow a flexible interest rate policy, so as to encourage domestic financial savings and more efficient use of bank credit. To achieve these objectives in the context of the envisaged liberalization of the trade and exchange system, the

Government will be raising the interest rate on savings deposits of one year or more by 5 percentage points (from 7 percent to 12 percent) with effect from July 1986. The structure of other interest rates (deposit and lending rates) will be adjusted accordingly. These adjustments will yield a real interest rate of 2 percent on savings deposits of one-year or higher maturity. The Government intends to continue this policy in the coming years.

IV. External Assistance Requirements

35. Burundi has made heavy use of external assistance, with foreign aid disbursements accounting for about 40 percent of total government resources, more than 60 percent of total investment, and 40-45 percent of import payments in recent years. Even under the most optimistic assumptions regarding the growth of exports and national savings, the country will continue to rely heavily on external assistance for the forseeable future. However, while external loan commitments increased substantially between 1976 and 1981 (from US$22.8 million to US$157.6 million), they have dropped to an average of less than US$90 million a year since 1982. External concessional loan commitments have followed the same trend: an increase from US$18 million in 1976 to US$126 million in 1981, falling to US$60-65 million a year during 1982-85. For the next three years, commitments of the major donors for project lending are expected to average US$70-75 million a year.

36. The financial program for 1986-89 assumes that world coffee prices will rise by about 50 percent to US$4.7 per kg in 1986, decline to US$4.05 per kg in 1987, and thereafter remain unchanged in nominal terms until 1990 and that average export prices for Burundi coffee will follow the same pattern; that coffee exports will increase from 34,000 tons in 1986 to 36,500 tons in 1988 (assuming that Burundi will be able to negotiate a quota with the ICO compatible with these levels); and that the reforms included in the program will result in higher growth of noncoffee exports, including manufactures. In this context, and taking into account the import needs associated with the objective of maintaining GDP growth at 4 percent, the external current account gap (excluding capital grants) is expected to average about SDR 72 million annually during 1986/89. As the Government's program also aims at building up the net official foreign assets to at least the equivalent of three months of imports, Burundi will need to mobilize annually about SDR 95 million in the form of net capital inflows. Net inflows from the existing pipeline are estimated to average SDR 45 million a year, and IDA (and African facility) nonproject lending is expected to amount to about SDR 23 million a year in 1986-87. Disbursements under the SAF are expected to amount to SDR 8.54 million in 1986 and about SDR 5.76 million in 1987 and 1988. Assuming that the major donors endorse the program, the remainder of the financing need (a net amount of about SDR 33.5 million a year) would need to be covered by new commitments from IDA and other donors.

37. While roundtable conferences of donors have been organized in the past for coordinating aid inflows to Burundi, there is still scope for improvement in this area. In the context of the proposed program, the Government will strengthen aid coordination among all major donors (including those without local representatives, such as the African Development Bank) to ensure that investment projects financed are included in the public investment program and that all external financing will be mobilized on concessional terms.

Burundi - Structural Adjustment Facility
Memorandum of Economic and Financial Policies
July 1, 1986 - June 30, 1989

1. During the three-year period from July 1, 1986 to June 30, 1989, the Government of Burundi has decided to implement a package of economic and financial policies that aims at both resolving the main structural problems and at correcting the serious domestic and external financial imbalances which Burundi has experienced since the early 1980s. These problems and the policies to be followed to resolve them are described in the document entitled "Medium-Term Economic and Financial Policy Framework." In support of the three-year program that the Government will be implementing during the period from July 1986 to June 1989, Burundi requests a structural arrangement from the Fund for a period of three years in the amount that will be available to Burundi under the Structural Adjustment Facility (currently projected at about SDR 20.07 million) and the first annual arrangement thereunder. Financial resources provided under the SAF will give us confidence to pursue vigorously the structural and investment policies aimed at improving the efficiency of the economy that will lay the foundation for a sustainable growth.

2. The Government's broad objectives of the three-year program are to raise the growth rate of real GDP from the low levels attained in the past four years, progress toward a viable balance of payments position, and achieve a progressive reduction in the domestic inflation rate. The target for the annual growth rate of real GDP is 4 percent. The domestic inflation rate is to be reduced from 10 percent in 1986 to about 7 percent by 1989. The balance of payments objectives are to contain the deficits in the external current account and the related foreign borrowing requirements to levels that will (a) ensure a reduction in the external debt service ratio (as a percentage of exports of goods and services, and private transfers) from 19.8 percent in 1985 to 18.5 percent by 1989; and (b) lead to the annual overall surpluses in the balance of payments required to raise net official foreign assets from the equivalent of 1.1 months of imports at end-1985 to at least the equivalent of three months of imports beginning end-1986. For the period 1986-89, on an average annual basis, these objectives imply an investment/GDP ratio of 16-19 percent (compared with 17.2 percent in 1982-85), and an external current account deficit/GDP ratio of 6 percent (compared with 8 percent in 1982-85).

3. To achieve these broad objectives over the next three years, major policy reforms will be implemented. These policy reforms will include: (a) flexible exchange rate management, trade and exchange control liberalization measures, and appropriate industrial policy changes; (b) measures to improve the quality of public development expenditures and efficiency of public enterprises; (c) improved incentives for agricultural production and exports; (d) measures to

increase domestic resource mobilization in the public sector; and (e) financial sector policy reforms (including a flexible interest rate policy) designed to ensure adequate growth in private savings and investment.

4. The annual program for 1986/87 (July 1986-June 1987, the first year under the SAF) will include the objectives and policy measures that relate to the first 12 months of the 18-month program (July 1986-December 1987) described in my letter dated May 19, 1986 and the memorandum of economic and financial policies attached thereto in connection with Burundi's request for a stand-by arrangement. For purposes of monitoring progress under the first annual program under the SAF we will follow closely developments in outstanding domestic credit, outstanding net claims of the banking system on the Government, the stock of the Government's domestic arrears, the contracting or guaranteeing of nonconcessional loans of 0-12 years by the public sector, the net official reserves, and the ratio of the overall deficit in central government operations to GDP, for which quantitative benchmarks have been established (Table 1). In view of the importance the Government attaches to achieving the fiscal objectives programmed for 1986 and 1987, the attached Tables 2 and 3 present targets for central government operations for the period from July 1986 to June 1987. Attainment of the targets for total expenditure, recurrent expenditure, overall deficit, cash reduction of domestic arrears, and net reduction of government indebtedness to the banking system will be closely monitored.

5. Policy implementation will also be closely monitored with reference to the benchmarks presented in Table 4, to ensure that timely actions of sufficient magnitude are taken with regard to (a) import and exchange control liberalization; (b) tariff reforms; (c) exchange rate adjustments and (d) rehabilitation of parastatals.

6. Burundi will provide the Fund with such information as the Fund requests in connection with the progress of Burundi in implementing the policies and achieving the objectives of the program, and the document entitled "Medium-Term Economic and Financial Policy Framework" (July 1, 1986-June 30, 1989) will be updated annually as the program is implemented. The Government believes that the policies set forth in this memorandum are adequate to achieve the objectives of its program but will take any further measures that may become appropriate for this purpose.

/s/ Pierre Ngenzi
Minister of Finance

Table 1. Burundi: Quantitative Benchmarks under the Structural Adjustment Facility, 1986-87

	1986		1987	
	Sept.	Dec.	March	June
	(In billions of Burundi francs; end of period)			
Total domestic credit	29.0	24.0	22.4	21.2
Net credit to Government	15.1	9.8	7.9	5.7
Cumulative reductions of domestic arrears by Government	1.0	1.86	--	--
	(In millions of SDRs)			
Minimum levels of net official foreign assets at end of period (excluding gold)	20.0	71.0	72.0	73.6
New nonconcessional foreign borrowing contracted or guaranteed by the public sector in the maturity range of:				
0 to 1 year 1/	--	--	--	--
1 to 12 years	--	--	--	--
	(In percent)			
		1986	1986/87 2/	
Ratio of the overall deficit in central government financial operations to GDP (including grants) 3/		-0.3	1.0	

1/ Excludes normal commercial credits.
2/ July 1, 1986-June 30, 1987. The deficit/GDP ratio is estimated on the basis of a nominal GDP estimate of FBu 168.7 billion.
3/ On a commitment basis.

Table 2. Burundi: Quarterly Cash Flow Plan of the Treasury, 1986-87

(In billions of Burundi francs)

	Quarterly objectives 1986					Quarterly objectives 1987				
	I	II	III	IV	Total	I	II	III	IV	Total
Revenue	4.60	6.34	7.04	11.39	29.37	8.24	7.08	6.30	8.40	30.02
Coffee	0.61	1.48	2.19	5.66	9.94	3.67	1.51	0.74	1.82	7.74
Other	3.99	4.86	4.85	5.73	19.43	4.57	5.57	5.56	6.58	22.28
Expenditures	4.43	4.14	4.40	4.29	17.26	4.67	4.35	4.63	4.53	18.18
Salaries	1.97	1.96	1.96	1.96	7.85	2.06	2.06	2.06	2.06	8.24
Goods and services	1.06	1.06	1.07	1.07	4.26	1.17	1.18	1.17	1.18	4.70
Transfers	0.58	0.27	0.62	0.51	1.98	0.63	0.28	0.66	0.54	2.11
Domestic	0.39	0.21	0.57	0.47	1.64					
External	0.19	0.06	0.05	0.04	0.34					
Other	0.12	0.12	0.12	0.12	0.48	0.13	0.13	0.13	0.14	0.53
Interest	0.70	0.73	0.63	0.63	2.69	0.68	0.70	0.61	0.61	2.60
Domestic	0.20	0.29	0.30	0.30	1.09					
External	0.50	0.44	0.33	0.33	1.60					
Amortization of external debt	0.69	0.60	0.47	0.46	2.22	0.90	0.77	0.61	0.60	2.88
Less reimbursements of principal payments	0.11	0.12	0.16	0.27	0.66					
Arrears reduction	--	0.50	0.50	0.86	1.86	--	--	--	--	--
Equipment and investment budget	0.75	0.75	0.75	0.77	3.02	0.76	0.76	0.76	0.77	3.05
Difference 1/	-1.16	0.47	1.08	5.28	5.67	1.91	1.20	0.30	2.50	5.91

1/ Reflects bank financing as programmed.

Table 3. Burundi: Central Government Operations, 1986-87

(In billions of Burundi francs)

	1986	1987	1986/87
Revenues and grants	35.16	36.75	40.01
Revenues	29.37	30.02	33.75
Coffee	(9.94)	(7.74)	(13.03)
Other	(19.43)	(22.28)	(20.72)
Grants	5.79	6.73	6.26
Expenditure and net lending (commitment basis)	35.68	40.88	38.18
Current expenditures	17.26	18.18	17.71
Salaries	(7.85)	(8.24)	(8.04)
Goods and services	(4.26)	(4.70)	(4.49)
Transfers	(1.98)	(2.11)	(2.04)
Interest	(2.69)	(2.60)	(2.64)
Other	(0.48)	(0.53)	(0.50)
Capital expenditures and net lending	18.42	22.70	20.47
Equipment and investment budget	(3.02)	(3.05)	(3.04)
Investments based on loans and grants	(16.06)	(19.65)	(17.86)
Less: reimbursements of principal payments by enterprises	(-0.66)	(--)	(-0.43)
Overall deficit (commitment basis)	-0.52	-4.13	1.83
Change in arrears	-1.86	--	-1.36
Overall deficit (cash basis)	-2.38	-4.13	0.47
Financing	2.38	4.13	-0.47
External	8.05	10.04	9.00
Drawings	(10.27)	(12.92)	(11.6)
Amortization	(-2.22)	(-2.88)	(-2.6)
Domestic	-5.67	-5.91	-9.47
Banking system	(-5.67)	(-5.91)	(-9.47)
Other	(--)	(--)	(--)

Table 4. Burundi: Benchmarks of Policy Implementation under the Structural Adjustment Facility

Policy measures	Dates
1. Liberalization of import and exchange controls	
- automatic granting of import licenses for all products except glass, textile and pharmaceutical products, and a few luxury items, which will remain subject to temporary controls;	Before August 1, 1986.
- the remaining quantitative restrictions on luxury items will be replaced by import tariffs;	Before end-1986.
- review of the restrictions on other products;	Before end-1986.
- with objective of eliminating or replacing them with appropriate tariffs;	Before end-1987.
- increase in the limits on outward foreign remittances.	First increase effective before end-June 1986; second increase effective January 1, 1987.
2. Comprehensive reform of the import tariff structure	
- consolidation of the import and fiscal duties, and establishment of a new range of tariffs.	Luxury products: 100 percent during 1986-87; Manufactured products: 50 percent in 1986, 45 percent in 1987, 40 percent in 1988-89; Food products: 25 percent during 1986-87; Intermediate goods and other primary products: 15 percent in 1986, 20 percent in 1987, 25 percent in 1988, 30 percent in 1989; and Equipment goods: 15 percent in 1986 and 20 percent during 1987-89.
3. Public enterprises	
- introduction of new tariffs for water and electricity	Before August 1, 1986.
- launching of rehabilitation program for the priority enterprises (CADEBU, ONAPHA, OTRABU, OTRACO, VERRUNDI)	July 1986.