EBS/86/227
Supplement 2

CONFIDENTIAL

November 25, 1986

To: Members of the Executive Board

From: The Secretary

Subject: Senegal - Structural Adjustment Arrangement

Attached for the records of the Executive Directors is the text of the structural adjustment arrangement for Senegal agreed at Executive Board Meeting 86/178, November 10, 1986.

Att: (1)

Senegal - Three-Year and First Annual Arrangements
Under the Structural Adjustment Facility

Attached hereto is a letter dated September 22, 1986 from the Government of Senegal, 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 November 1, 1986, Senegal will have the right to obtain three successive loans from the Fund under the Structural Adjustment Facility in a total amount equivalent to SDR 39,997,000.

2. The first loan, in an amount equivalent to SDR 17.02 million, is available for disbursement at the request of Senegal.

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 Senegal. The amount of the second loan will be equivalent to SDR 11,488,500, and the amount of the third loan will be equivalent to SDR 11,488,500.

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

(a) the indicators described in paragraph 23 of the annexed letter dated September 22, 1986 from the Minister of Economy and Finance,

(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 24 of the annexed letter dated September 22, Senegal will provide the Fund with such information as the Fund requests in connection with the progress of Senegal in implementing the policies and reaching the objectives supported by the first annual arrangement.

6. In accordance with paragraph 25 of the annexed letter dated September 22, Senegal will consult the Fund on the adoption of any measures that may be appropriate at the initiative of the Government or whenever the Managing Director requests consultation because he considers that consultation on the program is desirable. These consultations may include correspondence and visits of officials of the Fund to Senegal or of representatives of Senegal to the Fund.

Dakar, September 22, 1986

Dear Mr. de Larosière:

As you are aware, since mid-1983 the Government of Senegal has been making intensified adjustment efforts, with a view to achieving a viable external payments position consonant with the restoration of sustainable economic growth over the medium term. As a result, in the context of successive programs supported by use of Fund resources, as well as by other external assistance, steady and substantial progress has been made toward economic and financial adjustment; and, except for a minor and inadvertent excess in external borrowing at end-March 1986, all performance criteria of the programs through that date were observed. The economy has been progressively liberalized, agricultural production incentives have been strengthened, the Government's overall fiscal deficit has been reduced sharply, public enterprise reform has been accelerated, domestic credit expansion has been brought under control, and the external current account position has been improved. However, these developments have entailed considerable social costs, not only because of the strong measures introduced under the programs but also because of the policy adaptations that became necessary to cope with major unforeseen developments, notably shortfalls in exports of groundnuts and in government revenue.

2. After two years of stagnation, owing mainly to severe drought, Senegal's overall economic performance improved appreciably in 1985/86 (July-June), the last year of the program supported by the 18-month stand-by arrangement from the International Monetary Fund which expired on July 15, 1986. With the substantial increases in producer prices under the new agricultural policy and the return of good weather conditions, record food crops were harvested; and production of groundnuts increased significantly, though it remained well below the levels reached in the early 1980s. Therefore, given the progress registered in other sectors of the economy, the gross domestic product (GDP) is now estimated to have risen by slightly more than 4 percent in real terms in 1985/86, compared with an increase of 5 percent envisaged in the program and a decline of about 1 percent in 1984/85. Furthermore, the rate of inflation, as measured by the GDP deflator, was brought down from almost 12 percent to some 9 percent, the programmed level. At the same time, although the country's export earnings were considerably lower than initially projected (by roughly SDR 100 million), largely because of the sharp decline in world market prices of groundnut oil, the export shortfall was partly offset by lower imports of goods and services. Thus, the external current account deficit, excluding official grants, was actually reduced from SDR 413 million in 1984/85 to an estimated SDR 408 million in 1985/86, or from the equivalent of 16.9 percent to 13.2 percent of GDP, respectively. Including official grants, the current account deficit is estimated to have declined from 11.2 percent to 8.3 percent of GDP, but fell short of the target of 6.9 percent of GDP specified in the program.

3. To help limit aggregate demand to a level compatible with available resources, the fiscal program was tightened further in the

course of the year, as it became increasingly evident that the shortfall in government revenue in 1985/86 would be even larger than had been foreseen at the time of the third review under the last stand-by arrangement. While the factors behind the revenue shortfall, which was attributable mostly to lower receipts from customs duties and taxes on goods and services, have not yet been fully established, two major reasons seem to have contributed to the problem: the lagged effects of two years of economic stagnation on the tax base; and the decline in imports, partly as a result of the wait-and-see attitude adopted by some traders in anticipation of tariff reform. In the event, the revenue shortfall in relation to the initial estimate amounted to CFAF 19 billion, equivalent to 1.5 percent of GDP, placing great strain on the budget, especially in the last few months of the fiscal year. If it were not for the decision taken in connection with the third review to mobilize the bulk of the surpluses being generated by the oil refinery (SAR) in support of the budget, the revenue shortfall would have been of the order of CFAF 38 billion. Thus, although expenditure was kept below the programmed level, the overall fiscal deficit, on a commitment basis and including grants, is estimated to have amounted to 2.3 percent of GDP in 1985/86, compared with a targeted 1.4 percent of GDP and a deficit equivalent to 3.5 percent of GDP in 1984/85. Faced with this situation, as well as with delays in certain external aid disbursements, the Treasury could not meet all of its obligations around year end. In the circumstances, and notwithstanding the many urgent domestic needs, it was felt important to give priority to discharging Senegal's external debt service obligations. Accordingly, virtually all verified arrears on external debt service payments, which had reached CFAF 10.9 billion at end-December 1985, were liquidated by end-June 1986. By contrast, domestic arrears of the Government and public agencies were reduced by only a small amount over the year as a whole. Moreover, the Treasury could not effect on schedule certain repayments in respect of reclassified 1984/85 crop credits and ONCAD debt amounting to CFAF 5.6 billion and CFAF 4.0 billion, respectively; these amounts will be repaid in the context of the 1986/87 program.

4. Despite the substantial progress made during the past three years, Senegal still faces major structural and financial problems. The economy remains fundamentally weak and vulnerable, the rate of inflation is high, and the internal and external financial imbalances are unsustainably large. In addition, the sizable domestic and external debt weighs heavily on the government budget and the balance of payments. Conscious of the magnitude of these problems, the Government of Senegal is determined to pursue its adjustment efforts in the period ahead. Thus, in collaboration with the staffs of the International Monetary Fund and the World Bank, as well as with representatives of Senegal's principal bilateral creditors and donors, the Government has developed an overall policy framework for the three years 1986/87-1988/89 aimed at carrying forward the process of adjustment. This is an integral part of our Medium- and Long-Term Program of Economic and Financial Adjustment, covering the period 1985-92, which was endorsed at the first meeting of the Consultative Group for Senegal in December 1984.

5. As indicated in the policy framework paper, which was transmitted to you on September 19, 1986, the basic objectives of the program for 1986/87-1988/89 are: (a) to achieve an average annual rate of growth of real GDP of the order of 3.5 percent, which would help improve real per capita incomes, given the estimated increase in population of 2.9 percent per annum; (b) to continue to curb the annual rate of inflation, as measured by the GDP deflator, from the estimated 9 percent in 1985/86 to some 5 percent in 1988/89; and (c) to reduce further the external current account deficit, excluding official grants, from the estimated 13.2 percent of GDP in 1985/86 to around 6.6 percent of GDP in 1988/89. In this way, and barring unforeseen adverse developments, it is our expectation that by the end of the program period Senegal would be close to realizing an overall position and a structure of the balance of payments consistent with orderly relations with creditors. Meanwhile, Senegal will continue to maintain an exchange system which is free of restrictions on payments and transfers for current international transactions. The Government of Senegal will remain in close contact with the staffs of the International Monetary Fund and the World Bank on developments and progress in the implementation of the three-year program, and the policy framework paper will be updated annually as the program is implemented.

6. To attain the above-mentioned macroeconomic objectives, the Government intends to pursue two key strategies during the program period: promote private sector initiative through appropriate pricing and other incentive policies, particularly in agriculture and industry, while reducing its own direct involvement in production activities; and achieve greater efficiency in public resource management through improvements in the allocation and implementation of public investments, reform of the public enterprise sector, and strengthening of government finances. As part of the latter strategy, the Government's overall fiscal balance, on a commitment basis and including grants, will be turned from the estimated deficit of 2.3 percent of GDP in 1985/86 to a surplus of at least 1 percent of GDP in 1988/89. Furthermore, during the program period all currently verified domestic arrears of the Government and public agencies (CFAF 36.1 billion at end-June 1986) will be settled in an orderly manner, which, we are convinced, will have a highly favorable impact on economic growth; and net government borrowing from the domestic banking system will be reduced considerably, thus making loanable funds increasingly available to meet the financing needs of the private sector. As the operating results of a number of key enterprises are also expected to improve, shifting from deficit to surplus, gross domestic savings in terms of GDP are programmed to increase significantly, from an estimated 6.3 percent in 1985/86 to 10.5 percent in 1988/89.

7. In support of these objectives and policies to be pursued during 1986/87-1988/89, and the objectives and policies for the first year of this period as set out below, the Government of Senegal hereby requests from the International Monetary Fund a three-year structural adjustment arrangement in the amount that will be available to Senegal

under the Fund's Structural Adjustment Facility (SAF), and the first annual arrangement thereunder. In addition, the Government hereby requests from the Fund a one-year stand-by arrangement in an amount equivalent to SDR 34.0 million. In view of Senegal's resource needs, the Goverment has also sought and received assurances of continued financial support from its other major creditors.

8. Consistent with our medium-term policy framework, the program for 1986/87 has been designed to sustain the recent progress toward economic and financial adjustment. Accordingly, the basic objectives of the 1986/87 program are: (a) to achieve a real rate of economic growth of about 4 percent; (b) to curb the rate of inflation, as measured by the GDP deflator, from the estimated 9 percent in 1985/86 to less than 7 percent; and (c) to reduce further the external current account deficit, excluding official grants, from the estimated 13.2 percent of GDP in 1985/86 to some 9 percent of GDP. To these ends, the Government will continue to place emphasis on removing the structural impediments to economic growth and improving supply conditions, while restraining aggregate demand to a level compatible with available resources.

9. An important assumption of the 1986/87 program is that weather conditions will remain favorable and that a better groundnut crop will be marketed. Thus, assuming that the currently low export prices of groundnuts are more than compensated by the recovery in volume, and that there is a moderate growth in other exports, total export receipts are projected to increase by 13 percent in terms of SDRs in 1986/87. However, to achieve the programmed reduction of the external current account deficit, the total import bill expressed in SDRs should rise by only 1 percent; as the value of imported petroleum products is projected to decline by 24 percent, this would imply limiting the growth of non-oil imports to 7 percent in nominal terms. To attain this result, the policies and measures described below will be rigorously implemented.

10. Under the new agricultural policy, which was adopted in 1984, a number of far-reaching measures have already been implemented, and considerable progress has been made in several areas; but further measures are required to fully revitalize this key sector. Accordingly, in 1986/87 we will continue to give high priority to agricultural policy reform, with a view to expanding and diversifying domestic production, so as to increase exports and curb reliance on imports, especially of rice; at the same time, we will reduce government intervention and subsidies.

To encourage the development of groundnut production, in April 1985 we raised the producer price to a remunerative level consonant with medium-term growth. In the circumstances, despite the recent sharp drop in world market prices of groundnut oil, we opted to maintain the producer price unchanged for the 1986/87 season so as not to give conflicting signals to a major segment of the farming community. The prospective losses on groundnut operations in 1986/87, estimated at CFAF 11 billion, will be financed by the oil millers and the government budget. For the medium term, we will continue to provide groundnut producers with adequate incentives, while being mindful of trends in world market prices and financial constraints. In 1986/87 further steps will be taken to decontrol input distribution and marketing of groundnuts, as well as to rationalize the structure and management of the oil mills. To strengthen the groundnut sector, the Government has decided to implement the following measures for the 1986/87 season: permit the sale on a cash basis of up to 55,000 tons of high-quality seeds to supplement those already held by the farmers themselves or their organizations; fully integrate the two oil milling companies (SONACOS and SEIB); and transform one of their processing plants (at Djourbel) to carry out activities with a higher rate of return.

To promote food security, in 1986/87 the Government intends to vigorously implement its cereals plan, which has been prepared with assistance from the FAO and the World Bank, and endorsed by creditors and donors at a meeting held in Dakar in June 1986. While maintaining remunerative producer prices for cereals, measures will be applied to exploit better the country's agricultural potential for greater cereals production, improve farming techniques, further liberalize marketing arrangements, and develop the processing of coarse grains to respond to local consumer tastes. Meanwhile, to foster the shift in demand in favor of domestic cereals, the retail price of rice will be kept at its present level, providing a minimum nominal protection above import cost of 25 percent to producers of domestic coarse grains (other than rice). Finally, with the support of the World Bank and other creditors and donors, in 1986/87 the process of restructuring of rural development agencies will be continued, with a view to reducing costs and government subsidies.

11. The Government remains committed to reducing progressively the involvement of the Price Equalization and Stabilization Fund (CPSP) in rice operations and privatizing rice imports and internal distribution. Thus, as an initial step, the CPSP's monopoly on rice imports will be abolished with effect in December 1986, and its share in rice imports will be reduced by one fourth, or 85,000 tons on an annual basis. Depending on a satisfactory evaluation of the role of private importers, in consultation with the World Bank, the rice trade will be fully privatized in December 1987, except for the management of a security stock of 60,000 tons of rice which will remain the responsibility of the CPSP. Under the new system, the bulk of the surpluses generated by the rice sector will continue to be mobilized in support of the government budget. Meanwhile, part of the surplus to be generated by the rice sector in 1986/87 will be utilized by the CPSP to settle its remaining arrears to the Senegalese Treasury in respect of customs duties on rice imports made during the period August 1980-June 1986, which amount to about CFAF 10 billion. Furthermore, the CPSP will transfer to the Treasury an additional CFAF 6.3 billion before end-December 1986 to repay the 1985/86 crop credits outstanding at the central bank (BCEAO).

12. A fundamental element of the program for 1986/87 is the launching of a comprehensive industrial policy reform, designed to improve the competitiveness of the industrial sector and to make enterprises more fully responsible and accountable for their business decisions, while reducing the cost to the Government of administering industrial incentives. As part of this reform, the system of protection is being rationalized by basing it progressively on a reduced and narrowed band of harmonized tariffs so as to achieve a lower and more uniform level of effective protection over the period 1986/87-1988/89. The new tariff structure, which was approved on July 28, 1986, is as follows in comparison with the old:

	Old Rates	New Rates	
		1986/87	1988/89
Customs tariff	15	15	10
Low fiscal tariff	10	10	10
Normal fiscal tariff	40	30	20
Increased fiscal tariff	50	35	30
Special fiscal tariff	75	65	50

This phased reduction of tariffs is being coupled with a progressive elimination of quantitative restrictions on imports so as to expand the taxable base and thus improve government revenue performance over the medium term. Accordingly, all quantitative restrictions on imports were lifted, effective August 14, 1986, except for those on certain items where the restrictions would be eliminated as follows: packing papers and cardboard on October 1, 1986; construction materials, marble, and shoe parts on January 1, 1987; and agricultural products and stationery on March 1, 1987. The complete elimination of all quantitative restrictions on imports is to be achieved by January 1988. In order to stimulate industrial exports in a more rational manner, with effect on July 28, 1986 the Government has revised the export subsidy scheme, basing it on industrial value-added in international prices. Conscious of the costs involved in such a scheme and given the existing budgetary constraints, we have set the subsidy rate at a level of 25 percent, which will imply a total subsidy of CFAF 4-5 billion in 1986/87, compared with about CFAF 7 billion under the old scheme.

In the context of the planned reviews of the existing special agreements with a number of enterprises, beginning with calendar 1986, the Government will conduct annual audits of the operations of the oil refinery (SAR), the oil milling company (SONACOS), and the sugar company (CSS), so as to better assess their financial positions. In the case of the SAR and SONACOS, this will help the Government to ascertain the actual level of their surpluses. As for the CSS, which continues to receive a large subsidy from the CPSP, we are planning to advance renegotiation of the existing agreement with the company, with a view to eliminating the subsidy in the coming years.

13. The Government intends to pursue an energy policy geared toward developing local sources of supply and restraining energy consumption through appropriate pricing policies in order to limit the

oil import bill. Although world oil prices have declined sharply since late 1985, we have maintained the existing structure of domestic prices of petroleum products unchanged, except for a significant reduction effected in July 1986 in the prices of diesel and fuel oils used by the electricity company (SENELEC) to support its rehabilitation efforts and, more generally, to help promote the recovery and growth of the economy through reductions in electricity tariffs. There will be no further adjustments in energy prices and tariffs until a comprehensive audit of energy consumption is completed in consultation with the World Bank. This policy is fully consistent with our medium-term objectives of promoting economic growth and energy conservation, while giving due regard to the need to mobilize the prospective surpluses of the oil sector in support of the budget. On the basis of an average price of imported crude oil of about US$16 per barrel and an average exchange rate of CFAF 350 per U.S. dollar, it is now estimated that the SAR will generate surpluses (over and above those guaranteed to its private shareholders) totaling CFAF 45 billion in 1986/87, all of which will be passed on to the Treasury for the financing of programmed government operations; use of any additional surpluses that may be generated by the SAR will be determined in the context of the mid-term review of the program. In addition, the prospective surplus at the retail level in 1986/87, estimated at CFAF 6 billion, will be made available and used exclusively to finance budgetary operations under the special accounts of the Treasury.

14. During 1986/87 the Government will continue to implement the interim public investment program for 1985/86-1986/87, as agreed with the World Bank, which has been derived from the Seventh Plan for 1985/86-1988/89 and places greater emphasis on investments in support of directly productive and high-priority rehabilitation activities. Under this interim program, the share of the primary sector in total investment is to be raised from 22 percent (in the Sixth Plan) to 35 percent, while the combined share of the secondary and tertiary sectors will be reduced. In order to better monitor the financial implementation of the public investment program, a new budgetary process has been adopted beginning with the 1986/87 fiscal year. On this new basis, and for the first time, all public investment outlays have been integrated into the government budget, which will allow closer control of the domestic and external financing of the entire public investment program. Meanwhile, we have been carrying forward the reform of public investment programming, with a view to the adoption of a three-year "rolling" public investment program effective in July 1987. The first draft of this program is expected to be reviewed in consultation with the World Bank by end-September 1986 and the final draft should be ready for discussion with other creditors and donors by end-February 1987, in time for inclusion of its first year in the 1987/88 budget law. In this regard, it should be noted that, in line with the progressive withdrawal of the Government from direct involvement in production and trade, the ratio of public investment in the overall level of investment in directly productive activities will be reduced. Furthermore, public investment in relation to GDP will be kept at a level consistent with

the objectives of the adjustment program and public finance constraints. Finally, increasing priority will be given to investments in support of directly productive activities, as well as to the rehabilitation and maintenance needs of the key sectors. In view of Senegal's limited debt servicing capacity, projects will be selected not only on the basis of their impact on the growth of output and employment but also on their contribution to the programmed improvement of the external current account. We trust that the preparation of investment programs and projects along these lines will help to facilitate and increase donor support of the Government's efforts, and that the next meeting of the Consultative Group for Senegal, tentatively scheduled for February 1987, will serve as a major forum for mobilizing and coordinating external assistance to Senegal.

15. In line with the comprehensive strategy for parapublic sector reform, which was adopted in July 1985, the Government will intensify its efforts to liquidate or privatize certain public enterprises and to rehabilitate others. According to the guidelines set out in our plan of action, all public enterprises engaged in the production of commercial goods and services will be considered for divestiture, with priority being given to those in competition with the private sector and those which place a heavy burden on public finances. As a first step, it has already been decided that in 1986/87, out of the 62 enterprises identified for divestiture, 3 will be liquidated and 3 offered for sale to the private sector. As regards those enterprises that will remain in the Government's portfolio, a rehabilitation program will be carried out in each case, with assistance from the World Bank and other partners. As in the past, the program will be included in a formal agreement between the Government and the enterprise, i.e., either a contrat-plan or a lettre de mission. In 1986/87 contrats-plans are expected to be completed and signed for the electricity company (SENELEC), the national telecommunications company (SONATEL), the national postal office (OPCE), the housing company (SICAP), the public housing office (OHLM), and the oil milling companies (SONACOS/SEIB). In addition, lettres de mission are expected to be finalized and signed for four rural development agencies (SODAGRI, SODEVA, SODEFITEX, and SOMIVAC). A new policy aimed at reducing direct budgetary subsidies to the parapublic sector up to 20 percent by 1989/90 has been initiated; in this context, a 5 percent reduction from the 1985/86 level is programmed for 1986/87. The reconciliation of cross-debts within the public sector has recently been completed, and a schedule has been established for the orderly settlement of all verified arrears beginning in 1986/87.

16. While the rehabilitation of the parapublic sector should help improve public finances, the Government will also pursue a tight fiscal policy designed to maintain the momentum of fiscal adjustment in 1986/87. In particular, to help limit the growth of domestic demand, the overall fiscal deficit, on a commitment basis and including grants, will be reduced further, from an estimated CFAF 28 billion in 1985/86 to some CFAF 12 billion in 1986/87, or from 2.3 percent of GDP to 0.9 percent of GDP, respectively.

17. In 1986/87 the verified arrears of the Government and public agencies will be reduced by CFAF 14 billion to CFAF 22.5 billion, in accordance with the schedule set out in the annexed table on the proposed performance criteria; as indicated in this table, the reduction in arrears could be accelerated if external budgetary assistance is higher than programmed. However, even after settlement of an estimated CFAF 15 billion of crop credits, including those that could not be reimbursed by June 1986, the overall cash deficit of the Treasury in relation to GDP will be reduced slightly, from 3.3 percent in 1985/86 to 3.0 percent in 1986/87. Given the expected sources of domestic and external financing, including debt relief, net government borrowing from the banking system in 1986/87 will be much lower than the 1985/86 level.

18. To achieve the 1986/87 fiscal targets, resolute actions will be taken on both the revenue and expenditure fronts. In view of the difficulties experienced in 1985/86, we intend to intensify our efforts in 1986/87 to improve revenue performance through a series of measures, including a number of measures recommended by the recent Fund technical assistance missions. In this context, priority will be given to strengthening tax administration and collection, especially with regard to customs duties, turnover taxes, and industrial and commercial profit taxes, through a simplification of existing regulations and practices, as well as through a reallocation of staff in favor of assessment and audit. The computerization of certain important procedures (customs, VAT, and taxes withheld at the source) will be started in 1986/87 and completed in the next fiscal year. We will continue to pursue the efforts to recover tax arrears and to improve collection procedures so as to avoid future accumulations, particularly through a reduction of the lags between assessments and collection. We will also complete the studies on the reform of property taxation and on the establishment of a property tax register (test) for the Dakar region by December 1986, with a view to implementing the relevant recommendations in 1987/88. Furthermore, with effect in December 1986, an excise tax reform is envisaged, involving inter alia the substitution of certain specific taxes by ad-valorem duties. In addition, as indicated earlier, in 1986/87 the prospective surpluses of the SAR, totaling CFAF 45 billion, will be mobilized in support of the government budget; of this total, at least CFAF 11 billion will be collected by end-September 1986, CFAF 22 billion by end-December 1986, and CFAF 33 billion by end-March 1987. Where the customs administration is concerned, its human and material resources will be strengthened so that it can effectively discharge its responsibilities. As to the customs duties, we have enacted (as explained above) a new tariff involving a phased reduction of the rates, coupled with a progressive elimination of quantitative restrictions on imports; this reform is expected to be revenue neutral in 1986/87 and to contribute to an appreciable improvement of revenue performance in subsequent years. Regarding the various exemption schemes, which are a source of considerable revenue losses for the government budget, the existing legal and administrative provisions will be reviewed in order to limit the granting of exemptions and to ensure a better monitoring. Given the anticipated level of external grants, equivalent to CFAF 14.8

billion, in 1986/87 total revenue and grants are estimated to reach CFAF 267.5 billion, or 12 percent higher than the 1985/86 level; excluding grants, total revenue is expected to increase by 15 percent, the bulk of which is attributable to the mobilization of the surpluses of the oil sector in support of the budget.

19. On the expenditure side, strict controls will continue to be applied on both current and capital outlays. In 1986/87 the increase in current outlays, excluding scheduled interest on the government debt, will be limited to 3 percent, implying a significant cut in real terms. To this end, the wage bill will be kept to within CFAF 114 billion, only 2 percent above the 1985/86 level, by strictly limiting advancements and promotions, avoiding any general increase in wages and salaries, and reducing the total number of civil servants from 68,893 at end-June 1986 to about 68,000 at end-June 1987 essentially by refraining from filling vacancies created by retirees. In the years ahead, the Government will aim at further reducing civil service employment through accelerated retirement, redeployment of existing staff, rigorous control of new recruitment, and the containment of admissions to civil service training schools. In 1986/87 outlays on materials, supplies, and transfers will be allowed to increase by no more than 5 percent to CFAF 71 billion. In this context, as mentioned earlier, direct budgetary subsidies to the parapublic sector will actually be reduced by 5 percent. Additional expenditure-saving measures will include strict limits on consumption of electricity, water, and gas, as well as on the use of telephone and other communication services. The level of capital expenditure planned for 1986/87 is consistent with the objectives of our public investment program, which calls for an increase in such expenditure by 26 percent in nominal terms over last year's relatively low level. The deficit on the special accounts held with the Treasury in 1986/87 is expected to increase moderately, while the surplus of the treasury correspondents is likely to be significantly larger on account of the scheduled repayments of the CPSP by end-December 1986. Consequently, total expenditure and net lending are programmed to rise by 5 percent to no more than CFAF 279.3 billion in 1986/87.

20. To reinforce the fiscal program, and thus help attain the programmed reduction of the external current account deficit, the monetary authorities will pursue a prudent credit policy, without compromising the financing needs of the expected cash crops. In 1986/87 the increase in private sector credit, excluding crop credit, will be limited to 2 percent, the same percentage increase as in 1985/86. Consistent with the fiscal targets, the expansion in net bank credit to the Government will be limited to 3.5 percent, which compares with an increase of 12 percent in 1985/86. Therefore, and in order to better control total credit expansion, net domestic assets of the banking system relative to the level outstanding at end-June 1986 will be reduced by CFAF 7.4 billion by end-September 1986 and will rise by no more than CFAF 7.6 billion by end-December 1986, as shown in the annexed table. Within these overall limits, net bank credit to the Government will be reduced by CFAF 1.6 billion and will rise by no more than

CFAF 6.7 billion, respectively. Although the ceilings for the remainder of the program period will be established in the context of the mid-term review of the program, indicative limits for the whole of 1986/87 are also shown in the annexed table. The monetary authorities are taking further steps to strengthen the financial position of the banking system and to improve the allocation of credit to the economy. In 1986/87 the programs aimed at restructuring and rehabilitating two commercial banks, the BCS and the USBCI, will be carried forward. The USBCI's rehabilitation program involves a substantial reduction in its costs, mainly through a cutback in the wage bill and financial charges; in support of these efforts, the Government intends to on-lend to the USBCI a loan to be contracted from a foreign commercial bank, whose proceeds will be used exclusively to reduce the USBCI's liabilities with the BCEAO on which it is currently paying penalty interest of 24.2 percent. Moreover, to help ameliorate the liquidity position of banks, the Government will make minimum quarterly repayments totaling CFAF 12 billion in 1986/87 on account of the debts resulting from the liquidation of ONCAD. The Government will also repay the outstanding 1984/85 crop credits to the BCEAO of CFAF 6.0 billion by end-December 1986, in accordance with the schedule indicated in the annexed table.

21. The adjustment measures specified above, together with the improved prospects for groundnut production and oil import prices, should lead to an improvement in Senegal's external payments position in 1986/87. The external current account deficit, excluding official grants, is targeted to be reduced markedly, from SDR 408 million in 1985/86 to SDR 340 million in 1986/87, or from the equivalent of 13.2 percent of GDP to some 9 percent of GDP, respectively. After taking into account a modest increase in official grants and loan disbursements, scheduled amortization of public sector debt, repurchases from the Fund, and the liquidation of some small remaining arrears, the resulting financing gap is estimated at SDR 110 million in 1986/87. The gap is expected to be closed by the purchases under the requested stand-by arrangement, use of the Structural Adjustment Facility, and the rescheduling of debt service payments falling due to the Paris Club and other official creditors, on terms similar to those obtained in recent years. All verified arrears on nonreschedulable external debt service payments, including those accumulated since end-June 1986, will be eliminated by end-September 1986, and no external arrears will be incurred thereafter, as specified in the annexed table and under the assumption that the envisaged external budgetary assistance will be disbursed as scheduled. In the event that other arrears, external or domestic, are found to have existed as of end-June 1986, a schedule will be established for their elimination in an orderly manner.

22. The Government is aware of the need to pursue cautious external debt management policies so as to reduce the debt service burden over the medium term. Accordingly, as indicated in the annexed table, during the year ending June 1987 the Government will not contract or guarantee any external loans on nonconcessional terms, with an initial maturity from one up to (and including) 12 years, beyond a limit

equivalent to SDR 35 million; within this limit, loans from one up to(and including) 5 years will not exceed SDR 18.2 million. The latter amount relates to the loan which is expected to be used for the rehabilitation purposes of the USBCI, as described above; if this loan is not contracted, the borrowing ceilings will be reduced pro tanto. These limits will not include borrowings by the multinational companies Air Afrique and Agence pour la Sécurité de la Navigation Aérienne, or new borrowing for refinancing existing debts in the context of debt reschedulings. During the program period, there will be no short-term external borrowing (of less than 1 year) contracted or guaranteed by the Government, except for normal import-related credits.

23. As indicated above and shown in greater detail in the annexed table, to monitor progress under the program, the following quantitative performance criteria will apply: (a) ceilings on the cumulative change of net domestic assets of the banking system; (b) ceilings on the cumulative change of net bank claims on the Government; (c) a cumulative reduction of domestic payments arrears of the Government and public agencies; (d) elimination and avoidance of external payments arrears; (e) a cumulative repayment of crop credits; (f) a cumulative repayment of ONCAD debt; and (g) ceilings on new nonconcessional external loans contracted or guaranteed by the Government. The performance criteria for the remainder of the program period that are not specified in the annexed table will be established at the time of the mid-term review of the program to be completed by end-March 1987. In addition, the stand-by arrangement will include the standard clauses regarding the exchange and payments system which will also constitute performance criteria.

For the purposes of the first annual arrangement under the Structural Adjustment Facility (SAF), all of the above performance criteria and the indicative credit limits for 1986/87 as a whole will serve as benchmarks. Moreover, there will be the following benchmarks for the timetable of specific policy actions under the SAF: (a) formulation of an appropriate action program based on a study for the determination of producer prices of cereals (target date no later than March 1987); (b) abolition of the CPSP's rice import monopoly (December 1986); (c) elimination of quantitative restrictions on certain imports according to the established schedule (October 1986, January 1987, and March 1987); and (d) adoption of a three-year "rolling" public investment program (July 1987).

24. As regards the request for loans under the Structural Adjustment Facility, the Government of Senegal will provide the Fund with such information as the Fund requests in connection with the progress being made in implementing the policies and achieving the objectives of the program.

25. The Government of Senegal believes that the policies and measures described above are adequate to achieve the objectives of its program but will take any further measures that may become appropriate

for this purpose. The Government will consult with the Managing Director of the Fund on the adoption of any measures that may be appropriate, at the initiative of the Government or whenever the Managing Director requests such consultation. The Government will reach detailed understandings with the Fund on any further measures that may be needed in the context of the mid-term review of the program referred to above. During the mid-term review, progress in the implementation of the program will be assessed and understandings on additional measures will be reached, if necessary, especially in light of the outcome of the debt rescheduling arrangements; understandings will also be reached on the appropriate performance criteria for the remainder of the program period.

26. The Government remains convinced of the need to pursue its adjustment efforts in the medium term and, in this context, would appreciate the continued technical and financial support of the Fund.

Sincerely yours,

Mamoudou Touré
Minister of Economy and Finance

Attachment

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

Senegal: Proposed Quantitative Performance Criteria for 1986/87

	Stock at End-June 1986	Change from July 1, 1986 to end 1986 Sept.	Dec.	1987 March	June
	(In billions of CFA francs)				
Net domestic assets 1/ 2/ 3/	535.2	-7.4	7.6	...	10.2 4/
Claims on Government (net) 1/ 2/	142.1	-1.6	6.7	5.8 4/	5.0 4/
Arrears of the Government and public agencies					
1. Domestic	36.1	-3.6 5/	-6.6	-9.6	-13.6
2. External	0.4	-0.4 5/	-0.4	-0.4	-0.4
Repayment of 1984/85 crop credit	6.0	3.0 5/	6.0	6.0	6.0
Repayment of ONCAD debt	87.0	3.0 5/	5.0	9.0	12.0
		(In millions of SDRs)			
New external borrowing on nonconcessional terms by the Government or with government guarantee 6/					
1. Short-term (less than 1 year)		--	--	--	--
2. 1-5 years' maturity		--	18.2	18.2	18.2
3. 1-12 years' maturity		16.8	35.0	35.0	35.0

1/ The program assumes that Senegal will receive external budgetary assistance (excluding grants) of CFAF 15.5 billion during the period July 1-September 30, 1986 and of CFAF 44 billion during the period July 1-December 31, 1986. In the event that the external budgetary assistance (excluding grants) exceeds the above amounts, the changes will be reduced pro tanto, net of any budgetary assistance used to accelerate: (a) the repayment of reclassified 1984/85 crop credit; (b) the reduction of arrears of the Government and public agencies; and (c) the repayment of ONCAD debt. No adjustment to the changes will be made if the external budgetary assistance falls below the above amounts.

2/ The program does not envisage the receipt by Senegal of any exceptional external financial assistance during the period July 1-December 31, 1986 that would have the effect of improving the net position of the Government vis-à-vis the banking system. Should such assistance be received, however, the changes will be reduced pro tanto, net of any expenditure tied to such assistance.

3/ At end-September 1986, the variation in net domestic assets will be adjusted upward by the amount of the reclassified 1984/85 crop credit outstanding. The program envisages a reduction in crop credit of CFAF 9.5 billion during the period July 1-September 30, 1986 and an increase of CFAF 2.2 billion during the period July 1-December 31, 1986. In the event that the variation in crop credit is lower or higher than these amounts, the variation in net domestic assets will be adjusted downward or upward pro tanto. The program envisages that the Government will repay all the 1985/86 crop credit during the period July 1- December 31, 1986; in the event that part of the 1985/86 crop credit is reclassified at end-December 1986, the variation of net domestic assets will be adjusted upward by up to CFAF 3.5 billion.

4/ Indicative.

5/ The program assumes that Senegal will receive external budgetary assistance, including a grant, administered by the World Bank and estimated at CFAF 16.8 billion during the period July 1-September 30, 1986. In the event that the full amount is not received, the changes in arrears of the Government and public agencies, and in repayments of crop credit and ONCAD debt, will be adjusted to compensate for the shortfall up to a cumulative amount of CFAF 13 billion.

6/ The exchange rate applicable to these borrowings will be the rate of the SDR vis-à-vis the contract currency on June 30, 1986, as reported in International Financial Statistics. For debts directly contracted by the Government, the loan will count toward the ceiling on the date of signature. For debts guaranteed by the Government, the full amount of the loan will count toward the ceiling on the date of full or first partial guarantee, whichever is earlier. For the purposes of this ceiling, the length of the loan is deemed to be from the date of signature or the date that the loan enters into effect (whichever is later) until the last scheduled amortization payment. For the 1986/87 ceiling, remaining tranches under the loans signed by SOTEXKA and SOTRAC in 1985/86 will count toward the ceiling on the dates the guarantees on the remaining tranches become effective, and will be converted into SDRs at the exchange rates of June 30, 1985. Loans on concessional terms as defined by the OECD Development Assistance Committee are excluded from these ceilings.

Dakar, September 19, 1986

Dear Mr. de Larosière:

On behalf of the Government of Senegal, we are pleased to transmit herewith a policy framework paper, prepared in collaboration with the staffs of the International Monetary Fund and the World Bank, setting forth the Government's basic economic objectives for the next three years and the macroeconomic and structural adjustment policies designed to achieve them. These policies are an integral part of our Medium- and Long-Term Program of Economic and Financial Adjustment, covering the period 1985-92, which was endorsed at the first meeting of the Consultative Group for Senegal in December 1984.

We are forwarding today the same letter and attached paper to the President of the World Bank.

Sincerely yours,

Cheikh Hamidou Kane
Minister of Planning and Cooperation

Mamoudou Touré
Minister of Economy and Finance

Attachment

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

SENEGAL

Economic Policy Framework for 1986/87-1988/89

September 19, 1986

I. Introduction

After several years of increasing difficulties, in the late 1970s and early 1980s Senegal's structural and financial problems assumed disquieting proportions, and the country faced a serious and imminent payments crisis. On the whole, the economy registered little growth, with real gross domestic product (GDP) rising at a slower pace than the annual increase in population of 2.9 percent, internal imbalances widened markedly, and the external payments position came under mounting pressure. As in the case of many low-income countries in Africa, notably in the Sahelian region, Senegal's problems were attributable in part to exogenous factors, particularly recurring drought, declining terms of trade, the sharp increase in interest rates in international financial markets, the variability in exchange rates, and the rise in protectionism in industrial countries. However, they were also due largely to the inappropriate production, investment, and pricing policies pursued in the 1970s; these policies led to a considerable weakening of agricultural and industrial production incentives and to an overextension of the public sector. In addition, fiscal and credit policies were generally expansionary, and tended to favor consumption rather than productive investment.

As a result, in the five fiscal years ended in June 1983 domestic demand consistently exceeded supply, with the resource gap amounting on average to some 15 percent of GDP; gross domestic saving was very small and at times negative, while gross investment averaged almost 16 percent of GDP. To finance the high level of domestic demand, the public sector had substantial recourse to external borrowing; but such borrowing overtaxed the country's debt servicing capacity, and thus the Government of Senegal had to seek a series of debt reschedulings. Over the same five-year period the disbursed medium- and long-term public and publicly-guaranteed external debt rose almost threefold, reaching some SDR 1.3 billion, equivalent to 57 percent of the estimated GDP for 1982/83. Nevertheless, Senegal still incurred sizable overall balance of payments deficits, entailing an increase in the net foreign liabilities of the central bank (BCEAO) from SDR 48 million at end-June 1978 to SDR 400 million at end-June 1983. On the fiscal side, the growing imbalances could not be fully financed, leading to a large accumulation of domestic arrears. As of end-June 1983, verified domestic arrears of the Government and public agencies totaled CFAF 55.7 billion, or about 6 percent of GDP. Moreover, with the liquidation of a large rural development agency (ONCAD), beginning in August 1983 the Government had to ensure the servicing of this agency's debts to local banks valued at

CFAF 94.0 billion (excluding late interest and other charges), or more than 10 percent of GDP. Other public agencies and enterprises continued to face serious operational and financial difficulties.

II. Recent Adjustment Effort

In an effort to deal with the country's serious structural and financial problems, since 1980 the Government has adopted a number of adjustment programs which have been supported by use of Fund and World Bank resources, as well as by other external assistance, including external debt relief obtained through reschedulings negotiated with official creditors and commercial banks. Initially, the results achieved were mixed, not only because of the adverse impact of drought and the other exogenous factors already mentioned but also due to certain weaknesses in policy implementation. Thus, the program of economic and financial adjustment for 1980/81-1982/83, in support of which the Fund approved an extended arrangement in August 1980, ran into considerable difficulties at an early stage, and was subsequently replaced by annual programs. Similarly, the program supported by a structural adjustment loan and credit from the World Bank, which was approved in December 1980, was only partly implemented; and the second tranche of the loan was cancelled in June 1983. Under the Fund-supported program for 1981/82, a significant adjustment was made; but the improvement was not sustained, and the situation deteriorated again in the following year.

By contrast, since mid-1983 steady and substantial progress has been made toward economic and financial adjustment, as appropriate supply-side and demand management policies have been pursued with determination and adapted promptly to deal with unforeseen developments. The economy has been progressively liberalized, agricultural production incentives have been strengthened, government outlays relative to GDP have been reduced sharply, public enterprise reform has been accelerated, domestic credit expansion has been brought under control, and the external current account position has been improved. A particularly important achievement has been the major turnaround in the Government's fiscal performance, a key element of the adjustment effort; although the growth in revenue has lagged behind that of GDP, the overall fiscal deficit, on a commitment basis and including grants, was reduced from the equivalent of 8.2 percent of GDP in 1982/83 to 3.5 percent in 1984/85, and it is estimated to have been brought down further to 2.3 percent in 1985/86. This major fiscal adjustment, together with the favorable impact of policies and measures in other areas, helped to limit the external current account deficit, including official grants, to an estimated 8.3 percent of GDP in 1985/86, compared with 14.0 percent in 1982/83; excluding official grants, the external current account deficit was reduced from 18.4 percent of GDP in 1982/83 to an estimated 13.2 percent in 1985/86. However, economic growth has been slow, owing largely to the adverse impact of drought and continuing structural problems in several sectors.

III. Current Problems and Medium-Term Objectives

Despite the substantial progress made during the past three years, Senegal still faces major structural and financial difficulties. The economy remains fundamentally weak and vulnerable, government finances are precarious, the public enterprise sector is overextended, domestic arrears are substantial, and the external current account deficit is unsustainably large. In addition, the sizable domestic and external debt, the legacy of the expansionary policies pursued in the 1970s, weighs heavily on the government budget and the balance of payments. Scheduled external debt service payments are estimated to amount to 26-27 percent of exports of goods, services, and private transfers in 1986/87, as well as in each of the next two years.

In view of the magnitude of the existing problems, the Government of Senegal has decided to pursue the adjustment effort in the context of an overall policy framework for the three years 1986/87-1988/89 that has been developed in close collaboration with the staffs of the Fund and of the World Bank, as well as with representatives of Senegal's principal bilateral creditors and donors. This is an integral and essential part of our Medium- and Long-Term Program of Economic and Financial Adjustment, covering the period 1985-92, which was endorsed at the first meeting of the Consultative Group for Senegal in December 1984. As such, it is consistent with the program described in our Letter of Development Policy of December 19, 1985 to the International Development Association, in support of which the Association approved a financing package equivalent to about SDR 64 million.

The basic objectives of the program for 1986/87-1988/89 are threefold: (a) to achieve an average annual rate of growth of real GDP of the order of 3.5 percent, which would help improve real per capita incomes; (b) to continue to curb the annual rate of inflation, as measured by the GDP deflator, from an estimated 9.0 percent in 1985/86 to some 5.0 percent in 1988/89; and (c) to reduce further the external current account deficit, excluding official grants, from the estimated 13.2 percent of GDP in 1985/86 to around 6.6 percent in 1988/89. In this way, substantial progress would be made toward a viable external payments position consonant with the restoration of sustainable economic growth over the medium term. Indeed, it is our expectation that, barring unforeseen developments, by the end of the program period Senegal would be close to realizing an overall position and a structure of the balance of payments consistent with orderly relations with creditors, while continuing to maintain an exchange system which is free of restrictions on payments and transfers for current international transactions.

To attain these basic objectives, our overall policy framework encompasses two key strategies: the promotion of private sector initiative through appropriate pricing and other incentive policies, particularly in agriculture and industry, coupled with a progressive withdrawal of the Government and public agencies from direct involvement in production activities; and the achievement of greater efficiency in public resource management through improvements in the allocation and implementation of public investments, reform of the public enterprise sector, and strengthening of government finances. As part of the latter strategy, during the program period the Government's overall fiscal balance, on a commitment basis and including grants, will be turned from the estimated deficit of 2.3 percent of GDP in 1985/86 to a surplus of at least 1 percent of GDP in 1988/89; all currently verified domestic arrears of the Government and public agencies will be settled in an orderly manner; and recourse to domestic bank borrowing by the Government will be reduced considerably, thus making loanable funds increasingly available to meet the financing needs of the private sector. As the operating results of a number of key enterprises are also expected to shift from deficit to surplus, gross domestic savings in terms of GDP are programmed to increase significantly, from an estimated 6.3 percent in 1985/86 to 10.5 percent in 1988/89.

IV. Macroeconomic and Structural Adjustment Policies

Within the broad framework described above, the Government will implement a coherent set of supply-side and demand management policies designed to alleviate the macroeconomic and structural problems in the economy, thereby promoting balance of payments adjustment and economic growth. In 1986/87, the first year of the program, we intend to take strong actions in several important areas; but in this process, high priority will be given to the continued implementation of the new agricultural policy, which was adopted in 1984, industrial policy reform, and the reform of the parapublic sector. A summary and the time frame of our policies for the entire program period is provided in the attached table.

1. Public investment program

In the period immediately ahead, we will continue to implement the interim public investment program for 1985/86-1986/87, as agreed with the World Bank, which has been derived from the Seventh Plan for 1985/86-1988/89 and places greater emphasis on investments in support of directly productive and high-priority rehabilitation activities. At the same time, the reform of the public investment programming and budgeting process will be carried forward, with a view to the adoption of a three-year "rolling" public investment program effective in July 1987. A draft of this program is to be reviewed with the World Bank by end-September 1986 and should thus be ready for discussion with other creditors and donors by end-February 1987, in time for inclusion of its first year in the 1987/88 budget law. In this regard, it should be noted that, in line with the progressive withdrawal of the Government from direct involvement in production and trade, the ratio of public investment in the overall level of investment in directly productive activities will be reduced. Furthermore, public investment in relation to GDP will be kept at a level consistent with the objectives of the adjustment program and public finance constraints. Finally, in the selection of projects, increasing priority will be given to investments in support of directly productive activities, as well as to the rehabilitation and maintenance needs of the key sectors, while carefully evaluating the financing requirements and recurrent cost implications. Overall, projects will be selected not only on the basis of their impact on the growth of output and employment but also on their contribution to the programmed improvement of the external current account.

The preparation of appropriate investment programs and projects should help to facilitate and increase donor support of our efforts. In this regard, the Consultative Group for Senegal, together with the sectoral meetings held within its framework, should continue to serve as the major vehicle for the mobilization and coordination of development assistance to Senegal. In view of the country's limited debt servicing capacity, it is to be hoped that such assistance will progressively take the form of grants.

2. Agricultural policy

Under the new agricultural policy, a number of far-reaching measures have already been implemented, and considerable progress has been made in several areas; but further measures are clearly needed to fully revitalize this key sector. Accordingly, agricultural policy reform will continue to receive high priority, with a view to expanding and diversifying domestic production, thereby increasing exports and curbing reliance on imports, especially of rice; and also, reducing government intervention and subsidies.

To promote food security, we will vigorously implement our cereals plan, which was prepared with assistance from the FAO and the World Bank, and endorsed by creditors and donors at a meeting on agriculture held in Dakar in June 1986. With the abandonment of the past practice of rigid pricing and trading arrangements, more weight will be given progressively to economic factors in determining producer prices of cereals. In order to assure minimum acceptable rural incomes and to provide additional incentives to farmers, producer prices of cereals were increased significantly over the past two years. We are treating these prices as floor prices and intend to support them, if necessary, during a transition period until consumer demand for local cereals has developed sufficiently to absorb marketable surpluses of local grains. A study will be undertaken with World Bank assistance to develop a model to facilitate the determination of producer prices in future. On the basis of this study, which is expected to be completed during the first quarter of 1987, there will be an eventual review of producer prices of cereals to be put into effect in the 1987/88 growing season. Steps will also be taken to exploit better the country's agricultural potential for greater cereals production, improve farming techniques, liberalize progressively marketing arrangements for rice, and develop the processing of coarse grains to respond to local consumer tastes. At the same time, to foster the shift in demand in favor of domestic cereals, the retail price of rice will be kept at a level that will provide a minimum nominal protection above import cost of 25 percent to producers of domestic coarse grains (other than rice). The Government remains committed to reducing progressively the involvement of the Price Equalization and Stabilization Fund (CPSP) in rice operations and privatizing rice imports and internal distribution. Thus, as an intitial step, the CPSP's share in rice imports will be reduced by one fourth, or 85,000 tons on an annual basis, with effect in December 1986; a year later, and depending on a satisfactory evaluation in consultation with the World Bank of the role of private importers, the rice trade will be fully privatized, except for the management of a security stock of 60,000 tons of rice which will remain the responsibility of the CPSP.

To encourage the development of groundnut production, we intend to keep the producer price at a level that would continue to provide adequate incentives to farmers, while being mindful of world market trends and financial constraints; we will also decontrol input distribution and marketing, and rationalize the structure and management of the groundnut oil mills. Furthermore, although increased use of fertilizers will be encouraged, the Government's objective will be to decontrol gradually the marketing channels and eliminate reliance on subsidies which are currently being financed by donors. Finally, with the support of the World Bank and other creditors and donors, the restructuring of rural development agencies will be pursued.

3. Industrial policy

A fundamental element of our program is a comprehensive industrial policy reform designed to improve the competitiveness of the industrial sector and to make enterprises more fully responsible and accountable for their business decisions, while reducing the cost to the Government of administering industrial incentives. A number of important aspects of this reform will be put in place this year and others will be implemented during the period through 1988 with the following objectives. First, the system of protection will be rationalized by basing it progressively on a reduced and narrowed band of harmonized tariffs to achieve a lower and more uniform level of effective protection, and by phasing out quantitative restrictions on imports; the reductions in tariffs are being carried out in three stages, effective July 1986, July 1987, and July 1988. Second, export incentives are being increased in certain sectors, notably through the introduction in July 1986 of a revised export subsidy scheme based on industrial value-added in international prices, to improve the attractiveness of exporting relative to production for domestic sales. Third, government controls and administrative constraints burdening enterprises, as well as wage and labor law rigidities, will be examined with a view to their reduction or elimination. In addition, we will be reviewing the existing special agreements with certain enterprises, and henceforth we will be applying the general fiscal and trade laws to all enterprises engaged in commercial activities. These reforms are expected to lead to the restructuring and modernization of our industries, which, on the one hand, will be exposed to more international competition, but, on the other hand, will have better conditions and opportunities to face up to this challenge. We also believe that these reforms will encourage domestic and foreign investment, as well as foster labor mobility.

4. Energy policy

The Government will continue to pursue an energy policy geared toward developing local sources of supply, notably of hydroelectric power, and restraining energy consumption through appropriate pricing policies, with a view to limiting the oil import bill. Although efforts to expand local energy sources have not yet yielded any results, they are expected to bear fruit with the development of the hydroelectric power potential of the Manantali dam. The sharp reduction in world oil prices since late 1985 has had a highly favorable impact on the balance of payments, as well as on the financial position of the oil refinery (SAR). Consistent with the medium-term objectives of our energy policy, and the need to mobilize additional resources in support of the government budget, we have decided to maintain unchanged the existing structure of domestic prices of petroleum products, except for a significant reduction effected in July 1986 in those of diesel and fuel oils used by the electricity company (SENELEC) to support its rehabilitation efforts and, more generally, to help promote the recovery and growth of the economy through reductions in electricity tariffs. During the program period, we will continue to apply the present policy of maintaining domestic prices of petroleum products above those prevailing on world markets.

5. Fiscal policy

While placing a strong emphasis on removing the structural impediments to economic growth and improving supply conditions, the program will aim at restraining aggregate demand to a level compatible with available resources. Thus, the Government will maintain the momentum of fiscal adjustment over the medium term through the implementation of wide-ranging tax measures designed to increase the tax elasticity and ensure a durable revenue growth, combined with a spending policy aimed at curbing nonpriority expenditure and reallocating resources in line with development priorities. The resulting further improvement in government finances will not only ensure the liquidation of all currently verified domestic arrears but also improve the prospects for an orderly discharge of external debt service obligations.

To improve government revenue performance and make it more responsive to economic growth, we intend to implement a broadly-based program of action. This program is designed to increase revenue mainly by limiting exemptions to those envisaged by existing legislation, lowering those tax rates that encourage widespread evasion because of their excessively high level, and strengthening assessment and control procedures. To this end, most of the measures being studied by the National Commission for Tax Reform and those recommended by the recent Fund technical assistance missions will be implemented in 1986/87. Besides closing a number of loopholes, reforming the taxation of household income, revising the rate schedule of the general income tax, and reforming excise and property taxation, these measures aim at simplifying the existing legislation, streamlining collection procedures, reallocating personnel in favor of assessment and audit tasks, and restructuring the revenue departments to increase their efficiency. Our program of action also includes the revision of the customs tariff which, coupled with a progressive reduction of quantitative restrictions on imports, is expected to promote a sound industrial policy and improve revenue collection by deterring evasion and increasing the flow of imported goods passing through official channels. Moreover, the mobilization of the bulk of the profits now being generated by the oil sector in support of the budget should help improve revenue performance.

Concurrently, we will pursue a prudent spending policy, consistent with the need to generate adequate resources for financing the public investment program, clearing domestic arrears, and servicing the external debt. Measures to improve the allocation of available resources along clearly defined lines, including completion of a study on the sectoral and functional distribution of current expenditure, will be implemented in time for the preparation of the 1987/88 budget. In general, appropriations for outlays other than materials, supplies, and maintenance of essential services will be cut in real terms. Thus, the growth of the wage bill will be strictly limited through a freeze, and if necessary a reduction, of the total number of civil servants and a rationalization of administrative structures, coupled with a stricter stance with regard to promotions and merit increases; this will tend to reduce the share of the wage bill in the government budget. Subsidies and transfers will also be cut and, in particular, subsidies to public enterprises will be gradually terminated.

6. Parapublic sector reform

To enhance parapublic sector reform, so as to overcome the weaknesses in investment, savings, and budgetary performance, in July 1985 the Government adopted a comprehensive strategy involving two basic policy decisions: liquidation or privatization of certain enterprises; and rehabilitation of others. According to the guidelines set out in our plan of action, all public enterprises engaged in the production of commercial goods and services will be considered for divestiture, with priority being given to those in competition with the private sector and those that place a heavy burden on public finances. A number of enterprises eligible for divestiture have been identified, and the process of liquidation or privatization will be launched in 1986/87. As regards those enterprises that will remain in the Government's portfolio, a rehabilitation program is to be carried out in each case, focusing on: improvements in management, with increased autonomy and accountability; reduction and where possible elimination of subsidies, both direct and indirect; and simplification and strengthening of government supervision of the enterprise. As has been the recent practice, the program is to be included in a formal agreement between the Government and the enterprise, contained in a contrat-plan (or lettre de mission in the case of rural development agencies) defining their reciprocal commitments. Altogether, at least seven formal agreements with public entities are expected to be signed in the current fiscal year ending June 1987. In view of the problems of cross-arrears within the public sector, a reconciliation of the reciprocal obligations between the Government and the enterprises has recently been completed, and a schedule has been established for the orderly settlement of all verified arrears.

7. Monetary and credit policy

To reinforce the above measures, the monetary authorities will continue to pursue a prudent credit policy, without compromising the financing needs for the marketing of the cash crops and the desired revival of private sector activity. Further steps will also be taken to improve the financial position of the banking system, including the implementation over the next two years of programs aimed at restructuring and rehabilitating three commercial banks facing serious difficulties. In view of the targeted reduction in the external current account deficit and in the rate of inflation, we will be monitoring closely the increase in domestic liquidity. On the expectation that government recourse to bank borrowing will be gradually reduced, more credit will be allocated to the productive sectors of the economy. In the area of interest rate policy, which is common to all member countries of the West African Monetary Union, adjustments would be made when needed to take account of developments in foreign financial markets, as well as to foster financial savings and an efficient allocation of resources within the Union.

8. External debt management

In view of the heavy external debt burden, the Government will follow a very cautious external debt management policy, so as to limit debt servicing to manageable proportions. To this end, the Government will keep nonconcessional borrowing to a strict minimum in 1986/87 and beyond, while making intensified efforts to mobilize external assistance in the form of grants.

9. Social impact

The adjustment measures described above may entail an adverse social impact for some groups. However, the social costs are expected to be attenuated by a progressive orientation of current government expenditure toward the maintenance of social infrastructure and the provision of essential services. Moreover, they are expected to last for a relatively short period, until the adjustment measures take hold and economic performance improves. Overall, the social costs of the program, which are clearly unavoidable, are expected to be significantly smaller than those that would be incurred in the absence of an orderly adjustment process.

Senegal's economic situation and financial constraints necessitate reduction in real per capita consumption before an improvement is possible and sustainable. As much of this adjustment has already taken place since the early 1980s, current projections indicate that real per capita consumption should begin increasing in a few years. The adjustment program may also cause an income transfer between social and economic groups, but this is likely to favor the less advantaged, i.e., the rural communities, which represent the bulk of the population, relative to urban dwellers. Farmers' real incomes are already benefiting from the new pricing policies in agriculture, policies which are also addressing the key issue of ensuring a more balanced interregional development of the country. Urban areas have been bearing the cost of increased prices for basic commodities; they may also be adversely affected from the reduction in employment which may occur as inefficient firms face increased competition. In the medium term, however, new employment opportunities and improved earnings are expected, particularly as manufacturing firms respond to the industrial policy reforms under implementation. Although the speed at which this takes place is difficult to predict, the pattern of some adverse effects in the near term followed by generalized benefits in the medium and long term is typical of the expected impact of the program across most income groups.

V. External Financing Requirements

The effective implementation of the Government's macroeconomic and structural adjustment policies is expected to help strengthen Senegal's external payments position. In particular, the maintenance of appropriate price and other incentives should lead to a recovery in exports of groundnut products from the low levels registered in recent years, while contributing to a better performance of nontraditional exports. At the same time, the structural and demand-management measures should help promote import-substitution, especially in respect of foodstuffs. Thus, assuming no major changes in the current outlook for world commodity prices, the trade deficit is expected to narrow markedly; and the services and private transfers accounts together are projected to improve somewhat. Under this scenario, the current account deficit, excluding official grants, would decline steadily, from an estimated SDR 410 million in 1985/86 to SDR 290 million in 1988/89. Nevertheless, this would still involve total financing requirements for current transactions of the order of SDR 950 million over the three-year program period.

On the basis of recent and prospective flows of official grants and loans, total disbursements, mostly from traditional sources, are now projected to total about SDR 1.2 billion during 1986/87-1988/89. Of this total, taking into account operations already approved and new commitments to be confirmed, it is estimated that World Bank disbursements in the form of project and program loans will amount to about

SDR 170 million, including SDR 60 million in 1986/87. However, debt amortization, repurchases from the Fund, and an improvement in the operations account together are estimated to amount to SDR 640 million. Therefore, despite the expected improvement in the current account and the estimated net private capital inflows of approximately SDR 150 million, there would remain significant financing gaps over the period, although these are projected to decline from about SDR 110 million in 1986/87 to SDR 85 million in 1987/88 and further to SDR 65 million in 1988/89.

It is our expectation that, in the absence of any major external shocks, the financing gaps could be closed primarily through debt rescheduling arrangements along the lines of those concluded in recent years. Senegal will also be requesting shortly a one-year stand-by arrangement from the Fund in an amount equivalent to SDR 34 million; in addition, SDR 40 million is expected to be available over the next three years from the Structural Adjustment Facility (SAF). In 1986/87 purchases under the stand-by arrangement, together with use of the SAF, are estimated to amount to about SDR 43 million; the remaining financing gap of some SDR 67 million is expected to be covered by debt rescheduling from official creditors, which will be sought on terms similar to those obtained in recent years.

Table 1. Senegal: Summary and Time Frame for Macroeconomic and Structural Adjustment Policies, 1986/87-1988/89

	Objectives and Targets	Strategies and Measures	Timing of Measures 1/
1. Agricultural policy reform	Expand and diversify domestic production, and reduce government intervention and subsidies.	Continue the process of reform envisaged in the new agricultural policy.	1986/87, 1987/88, and 1988/89
a. Cereals policy	Promote food security, and reduce reliance on rice imports.	Adopt cereals plan.	July 1986
		Complete study to determine future producer prices of cereals.	March 1987
		Maintain remunerative producer prices for cereals, develop processed products responsive to consumer tastes, and keep a minimum nominal protection above import cost of 25 percent for domestic cereal production by adjusting, when necessary, the retail price of rice.	1986/87, 1987/88, and 1988/89
	Progressively privatize rice imports and internal distribution.	Abolish system of prior licensing and selection of local rice distributors, and assure distributors sufficient margins to cover transportation costs.	July 1986
		Initiate reduction in the share of the CPSP in rice imports.	December 1986
		Following an evaluation of performance under the new import system, fully privatize rice trade, except for security stock to be managed by CPSP.	December 1987
b. Groundnut sector	Foster production and reduce government intervention.	Maintain remunerative producer prices.	1986/87, 1987/88, and 1988/89
		Rationalize marketing, pass financial responsibility on to the oil millers, and fully merge SONACOS with SEIB.	1986/87
c. Rural development agencies	Restructure and rehabilitate key agencies.	Finalize and sign lettres de mission for SODAGRI, SODEVA, SODEFITEX, and SOMIVAC.	1986/87
2. Industrial policy reform	Rationalize the system of protection.	Lower existing rates and harmonize tariffs in three stages so as to achieve a lower and more uniform level of effective protection, which, combined with the progressive elimination of quantitative restrictions, would also help improve revenue performance.	July 1986, July 1987, and July 1988
	Increase export incentives.	Introduce revised export subsidy scheme based on industrial value added in international prices.	July 1986
	Apply the general fiscal and trade laws to all registered enterprises.	Review special agreements with certain major enterprises.	1986/87
	Improve business environment, and foster labor mobility.	Review wage and labor law rigidities and controls or constraints burdening enterprises, with a view to their reduction or elimination.	1986/87 and 1987/88

1/ Where a single date is indicated, it means that the measure(s) will be in effect no later than that date; where one year or several years are noted, it means that action will be taken in each year.

3. Energy policy	Develop local sources of supply and restrain energy consumption.	Maintain a structure of retail prices consistent with energy conservation and budgetary requirements.	1986/87, 1987/88, and 1988/89
4. Investment programming	Place greater emphasis on directly productive and high-priority rehabilitation activities.	Introduce appropriate public investment program for 1986/87.	July 1986
		Adopt appropriate three-year "rolling" public investment program.	July 1987
	Evaluate carefully financing requirements and recurrent cost implications of projects.	Strengthen capabilities of Planning Ministry.	1986/87, 1987/88, and 1988/89
5. Parapublic sector reform	Promote the efficiency of the parapublic sector, and reduce government intervention and subsidies.	Liquidation or privatization of public enterprises in competition with the private sector in the production of commercial goods and services.	1986/87, 1987/88, and 1988/89
		Finalize and sign contrats-plans for SENELEC, OPCE, SONATEL, SICAP, OHLM, and SONACOS/SEIB.	1986/87
	Progressively eliminate all verified cross-arrears.	Reconcile reciprocal obligations between the Government and the enterprises; and establish a schedule for the orderly settlement of all verified arrears.	1986/87, with settlement over three years
		Reduce and preferably eliminate operating subsidies to parastatals, according to an agreed plan.	1986/87, 1987/88, and 1988/89
6. Fiscal policy	Achieve a turnaround in the Government's fiscal operations, on a commitment basis and including grants, from deficit to surplus.	Improve revenue performance and pursue a prudent spending policy.	1986/87, 1987/88, and 1988/89
a. Revenue	Improve revenue performance.	Implement the recommendations of the National Commission for Tax Reform and recent Fund technical assistance missions:	1986/87, 1987/88, and 1988/89
		- Reform direct tax code.	1986/87
		- Revise customs tariff in three stages.	July 1986, July 1987, and July 1988
		Mobilize the prospective surpluses of the oil sector in support of the budget.	1986/87, 1987/88, and 1988/89
b. Expenditure	Maintain tight limits on current government outlays.	Control the wage bill by freezing or reducing the number of government employees, while developing proposals for a civil servants' resettlement fund; also keeping wage drift to a minimum.	1986/87, 1987/88, and 1988/89
		Reduce government subsidies and transfers.	1986/87, 1987/88, and 1988/89
		Make adequate provisions for materials, supplies, and maintenance of essential services.	1986/87, 1987/88, and 1988/89

Domestic arrears	Gradually eliminate all currently verified domestic arrears of the Government and public agencies.	Allocate adequate resources to liquidate such arrears.	1986/87, 1987/88, and 1988/89
7. Credit policy	Increase and improve credit to the private sector, while reducing net government borrowing from the banking system.	Strengthen the existing credit information structure	1986/87, 1987/88, and 1988/89
	Improve financial position of the banking system.	Restructure and rehabilitate three banks facing serious difficulties (BCS, BNDS, and USBCI).	1986/87 and 1987/88
	Discourage capital flight, mobilize domestic savings, and improve resource allocation.	Follow a flexible interest rate policy	1986/87, 1987/88, and 1988/89
8. External debt management	Limit external debt service burden to manageable proportions; and re-establish orderly relations with creditors.	Keep new external borrowing on nonconcessional terms to a strict minimum, while intensifying efforts to mobilize resources in the form of grants.	1986/87, 1987/88, and 1988/89
		Make adequate provisions for the prompt settlement of debt service obligations so as to avoid any external arrears.	1986/87, 1987/88, and 1988/89