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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 87/179

10:00 a.m., December 23, 1987

R. D. Erb, Acting Chairman

| Executive Directors | Alternate Executive Directors |
|---|---|
| A. Abdallah | E. T. El Kogali |
| | Jiang H. |
| | E. L. Walker, Temporary |
| | A. Rieffel, Temporary |
| | J. Prader |
| | E. V. Feldman |
| M. Finaish | A. M. Othman |
| | B. Goos |
| | A. Iljas, Temporary |
| A. Kafka | J. Hospedales |
| | C. Enoch |
| | G. D. Hodgson, Temporary |
| | C. V. Santos |
| | I. A. Al-Assaf |
| | C. Noriega, Temporary |
| | M. Fogelholm |
| | M. A. Kyhlberg, Temporary |
| H. Ploix | |
| G. A. Posthumus | G. P. J. Hogeweg |
| | C.-Y. Lim |
| | M. A. Hammoudi, Temporary |
| | S. Rouai, Temporary |
| | B. Tamami, Temporary |
| | L. E. N. Fernando |
| | A. Vasudevan, Temporary |
| | N. Adachi, Temporary |
| | N. Kyriazidis |
| | S. Rebecchini, Temporary |

L. Van Houtven, Secretary and Counsellor
M. J. Miller, Assistant

Also Present

IBRD: R. V. Key, Africa Regional Office. African Department: E. L. Bornemann, Deputy Director; E. A. Calamitsis, Deputy Director; D. J. Donovan, K. G. Dublin, C. Enweze, U. R. Gunjal, J. M. Jiménez, A. Oloyede, C. L. Rothman. European Department: G. H. R. Tersman. Exchange and Trade Relations Department: E. Brau, A. P. De La Torre, K. Flug, B. C. Stuart. External Relations Department: D. D. Driscoll. Legal Department: H. Elizalde, A. O. Liuksila, J. M. Ogoola, J. V. Surr. Research Department: G. R. Le Fort. Western Hemisphere Department: S. T. Beza, Director; M. E. Bonangelino, L. L. Pérez, R. K. Rennhack. Advisors to Executive Directors: P. E. Archibong, A. G. A. Faria, A. R. Ismael, G. Pineau, K. Yao, J. E. Zeas. Assistants to Executive Directors: R. Comotto, M. Hepp, S. King, V. K. Malhotra, J. A. K. Munthali, L. M. Piantini, G. Schurr, R. Wenzel, C. C. A. van den Berg.

1. THE GAMBIA - STRUCTURAL ADJUSTMENT FACILITY - SECOND ANNUAL ARRANGEMENT; AND EXCHANGE SYSTEM

The Executive Directors considered a staff paper on The Gambia's request for the second annual arrangement under the three-year structural adjustment arrangement approved on September 17, 1986 (EBS/87/236, 11/19/87). They also had before them a policy framework paper on The Gambia (EBD/87/300, 11/19/87).

The Acting Chairman made the following statement:

> There follows for the information of Executive Directors the text of a memorandum that I have received from the President of the World Bank to serve as the basis for my statement on the matter to the Board. This text summarizes the main points covered by the Executive Directors of the Bank and IDA in their December 8, 1987 discussion in Committee of the Whole of a paper entitled "The Gambia - Policy Framework Paper, 1987/88-1989/90."
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> 1. The Executive Directors commended the Government of The Gambia for its timely implementation of a comprehensive package of mutually reinforcing measures designed to lay the basis for sustained economic growth together with financial stability. They noted that The Gambia's economic and financial performance in the past year was better than originally anticipated in the Economic Recovery Program, and that the growth target of the future program has consequently been raised. The Directors noted, and expressed their support for the Government's commitment to continuing the reform process as outlined in the Policy Framework Paper.
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> 2. The questions and observations of the Executive Directors focused on five main sets of issues:
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> (a) growth prospects for the economy, including the dependence on groundnuts;
> (b) balance of payments viability;
> (c) the proposed taxation and resource mobilization measures;
> (d) the social impact of adjustment; and
> (e) the impact of The Gambia's adjustment on neighboring countries.
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> 3. Future growth prospects are fragile, and the staff noted that the Government is seeking to address the specific sectoral constraints to growth through the reform program. At the same time, the Government's development strategy relies on the willingness of the private sector to take the lead in directly productive activities. So far the private sector response has been encouraging, with substantial recent investment in tourism and fisheries. A specific concern regarding growth prospects relates to The Gambia's dependence on groundnut production, which is vulnerable to movements in international prices. The consensus was that

major but cautious efforts should be made in the next few years to diversify agricultural production, for example, into horticulture, as the agricultural sector will remain the most important source of growth in the foreseeable future. Efforts should continue to encourage private sector participation in other productive activities, particularly fisheries and tourism. The Executive Directors noted the difficulty of achieving rapid per capita income growth in a situation where population continues to grow by 3.2 percent annually.

4. The Executive Directors noted the strengthening of The Gambia's balance of payments position in recent years, and expressed support for further strengthening as envisaged in the program. There were questions regarding the size and sustainability of the current account deficit and the implications for future external capital needs. The balance of payments position is, despite recent improvements, still precarious, and the sustainability of the balance of payments depends on both continued reforms by Government, and active programs of donor support, and private capital inflows. The Directors noted that longer-term assistance flows to The Gambia should support continued development in the human resources and infrastructure sectors.

5. The Executive Directors discussed the resource mobilization component of the adjustment program. There was support for the introduction of the general sales tax, given the need for achieving greater financial balance, though one Director expressed concern that the shift from import taxes to a general sales tax might prove regressive, inflationary, as well as harmful to some local producers.

6. The Directors raised some questions regarding the social costs of the adjustment process, and indicated their hope that these would not delay the adjustment program. Regarding the high job losses associated with the retrenchment of the civil service, some Directors emphasized that while they supported the civil service reform, sufficient assistance should be provided to minimize the short-term adverse impact of policy reforms. It was noted that substantial labor absorption is occurring as a result of the recovery of the economy, government/donor assisted training and credit programs, and the promotion of labor-intensive activities; and that the Government has protected spending on basic social services and intends to continue to do so in the future.

7. One Executive Director raised a question regarding the impact of The Gambia's adjustment efforts on neighboring countries. The staff noted that The Gambia's adjustment program, aided by flexibility in the exchange rate, has helped The Gambia to adjust more quickly than other countries. The Bank should nonetheless remain committed to the principle of full adjustment by whatever policy tools are available to individual countries.

Mr. Abdallah made the following statement:

The Gambian authorities have been successful in implementing the first year of their Economic Recovery Program (1985/86-1987/88). As a result of the strong and comprehensive adjustment measures under that program, the Gambian economy has been able to record significant progress in reducing internal and external imbalances and laying the basis for a rapid and sustainable rate of economic growth in the medium term. Thus, real GDP rebounded impressively in 1986/87 with a growth of 6.1 percent, which reflected, in part, producer response to economic incentives and favorable weather conditions. This recovery was broad based and underscores the success of the authorities' diversification efforts. In extending the three-year program, the authorities now expect to achieve an average annual rate of growth of from 3.5 to 4.0 percent, compared with the initial target of 3.3 percent. At this rate of growth, some modest recovery in real per capita income and consumption could be achieved.

The Gambian economy has also witnessed a substantial deceleration in the rate of inflation, from about 70 percent at the end of 1985/86 to 20 percent by 1986/87, despite the effects of a sharp depreciation of the domestic currency early in 1986. The authorities expect to make further progress in this area, and have targeted a reduction in inflation, to 8 percent, by 1989/90. In the meantime, despite strong expenditure restraints accompanied by revenue-raising measures, the apparent widening of the budget deficit to 21.3 percent of GDP from a target of 17.5 percent in 1986/87 reflected the assumption by the Government of the loans guaranteed by the Gambia Commercial and Development Bank. As indicated by the staff, this had been agreed upon in the original stand-by arrangement but had not been included in the budget figures. It is worth noting, however, that the underlying fiscal adjustment is taking place as strong measures continue to be implemented. These have included a retrenchment of personnel in the Civil Service, amounting to about 20 percent of total employment, and continued reductions of subsidies to state enterprises through rehabilitation and divestiture. Nonetheless, the higher than envisaged disbursement of external assistance associated with the recovery program placed the Government in a net creditor position with the banking system.

In the external sector, the current account deficit widened, to 33.6 percent of GDP against the target of 32.6 percent, due to lower than expected export receipts and a strong rebound of imports in line with the upsurge in economic activity. With an increased disbursement under the World Bank's Structural Adjustment Credit, The Gambia was able to accelerate its reduction of external arrears. Furthermore, gross reserves were increased to the equivalent of 2.3 months of imports, compared with an initial target of only one month.

The Gambian authorities are continuing with their adjustment efforts as enunciated in the original policy framework paper. They recognize that much remains to be done to achieve sustainable growth and a viable balance of payments position. The long-run growth prospects continue to be constrained by a narrow productive base, while external viability requires the removal of systemic obstacles. Thus, in updating the three-year program, the authorities are determined to pursue the policies that had been endorsed by the Board in the original policy framework paper. The program for the second year under the structural adjustment facility (1987/88), together with the updated policy framework paper (1987/88-1989/90) has been clearly set out in the two staff papers before the Board. The remainder of this statement will highlight the thrust of these measures.

The flexible exchange rate policy remains central to the program, and the floating system based upon an interbank market has worked successfully thus far and has resulted in further depreciation of the dalasi to D 11.85 per pound sterling, following the initial devaluation from D 5 to D 10 per pound sterling. The effects of these exchange rate adjustments have been allowed to work through the domestic price mechanism, leading to the adjustment of the few remaining administered prices, e.g., premium gasoline (103 percent), gas-oil (40 percent), water tariffs (15 percent), electricity rates (9 percent), and bus fares (40 percent). Other price adjustments of these and other commodities will be made whenever necessary. Meanwhile, producer prices are being aligned to closely reflect world market prices and, for the 1987 season, groundnut prices have been reduced by 17 percent. This has also had the benefit of reducing the amount of the government subsidy. Other measures affecting the groundnut sector include continued liberalization of domestic marketing of the crop, as well as streamlining of credit. Other sectors should be able to benefit from the revised investment code, continuing divestiture, and price liberalization policies.

The budget deficit is expected to be reduced by 2.4 percentage points of GDP in 1987/88, and the authorities have set a target deficit of about 5 percent in 1989/90, which will be achieved through a combination of expenditure restraint and revenue-raising measures. In 1987/88, revenues should be strengthened by the tightening of tax administration, the introduction of a general sales tax, and the reform of the income tax law. However, the main thrust of fiscal adjustment would be achieved through elimination of the subsidy to the Gambia Produce and Marketing Board and continued rationalization and divestiture of public enterprises. At the same time, selection of capital projects will be subjected to more rigorous analysis and appraisal to ensure more efficient utilization of resources.

Monetary and credit policies are aimed at reducing further inflationary pressures, mobilizing domestic financial resources, and attaining the balance of payments objectives. To that effect, quantitative benchmarks will be closely monitored to ensure that monetary aggregates follow the predicted path of adjustment. At the same time, interest rate policy will remain flexible and will reflect the interplay of market forces.

As already pointed out, the authorities recognize that the balance of payments remains vulnerable. Accordingly, for the medium term, it is intended to continue mobilizing foreign assistance on highly concessional terms. It is hoped that by implementing the pragmatic policies under the program and the normalization of relations with all its creditors, The Gambia will be in a position to attract the required financing.

In conclusion, I would like to request Directors to approve the proposed decision as set out on page 27 of EBS/87/236, and to endorse the updated policy framework paper contained in EBS/87/300.

Mr. Enoch made the following statement:

The staff papers on The Gambia speak for themselves, and I therefore have little hesitation in endorsing the staff appraisal and the proposed decisions. The program for the second year of the structural adjustment arrangement is a welcome continuation of The Gambia's exemplary adjustment effort. There is much to commend in the actions of the Gambian authorities, and I will mention just a few items: first, the reduction of producer prices for groundnuts by 16.7 percent for the 1987/88 season, implying a halving of the producer subsidy; second, the proposals for liberalizing the groundnut market; third, the revised investment code; and fourth, the moves to encourage the development of fisheries and tourism as export earners in addition to the traditional production of groundnuts.

There have been some slippages from the objectives of the original policy framework paper but these have been quite minor and have not jeopardized the overall progress of The Gambia's Economic Recovery Program. The overall success of The Gambia's policies and performance over the past year has enabled the updated policy framework paper to be more ambitious than the earlier one in some of its targets. The growth target is raised from 3.3 percent to 3.5 to 4.0 percent, and inflation is to be brought down to 8 percent, rather than 10 percent, as originally envisaged. There is now also the prospect of no further debt rescheduling, of the elimination of external arrears, and some buildup of reserves. We continue to urge the authorities to be resolute in their efforts, not least as The Gambia still has some way to go in achieving medium-term economic viability. I note that the revised policy framework paper envisages a current account deficit of 24.5 percent of GDP in 1989-90, even higher than the 22 percent envisaged earlier. Deficits of this magnitude illustrate clearly the precariousness of the Gambian recovery. Unless they can be significantly reduced beyond this period, they are bound to become a significant constraint on The Gambia's growth prospects. The authorities must continue to seek to diversify their sources of export revenue, even though major progress will not be easy. In addition to encouragement of fisheries and tourism, agricultural diversification must also be central. In addition, as was pointed out in the discussion on The Gambia in August (EBM/87/127, 8/31/87), the authorities need to pay attention to resolving the problems giving rise to a multiple currency practice.

One difficulty I have with the revised policy framework paper is the misalignment between the structural adjustment arrangement program year and the authorities' fiscal year, which has led to a situation in which benchmarks are specified only up to June 1988. I would not make too much of this in the case of The Gambia, given that there can be little doubt about the authorities' commitment to the program, but in general we have argued that such a foreshortening in programs should be avoided. I believe the staff may be thinking of a partial realignment of the next structural adjustment arrangement program year and the fiscal year by advancing the former to September 1988, and this could be helpful. One alternative solution might be the conversion of the arrangement from the existing structural adjustment facility to the enhanced structural adjustment facility in order to utilize the flexibility possible under the new facility, with the midyear review.

Finally, I wish to repeat the requests made by this chair in August that the policy framework paper should address itself to banking sector reform, and should provide some regional perspective on questions such as groundnut producer prices. I would be interested in any staff comments on progress in collecting public sector arrears.

Mrs. Ploix made the following statement:

The staff paper confirms the general improvement of the Gambian economy that the Board already noted last August. We welcome the authorities' intention to further pursue their adjustment efforts, and we are also pleased that they attach importance to strengthening fiscal revenues in 1987/88 through such measures as implementing a general sales tax and reforming the income tax law. Other policy measures which are retained as structural benchmarks for this second annual arrangement under the structural adjustment arrangement are of major importance, namely, the revised investment code, and the performance contracts to be signed with several major public enterprises. We therefore support the proposed decisions, but would like to offer a few comments.

First, regarding the Fund's involvement in this program, it is disquieting to note that in 1987/88, net Fund financing (excluding from the structural adjustment facility) will be reduced by SDR 3 million, as structural adjustment facility resources (SDR 5 million) will be partly offset by a reimbursement of SDR 3 million under the tranche policies. This is contrary to our basic convictions about the nature of the structural adjustment facility; I wish to reaffirm our commitment to maintaining the additionality of structural adjustment facility resources. A new stand-by arrangement would have been both financially and technically justified for The Gambia, as Fund exposure under tranche policies (74 percent of quota) is quite modest.

Second, regarding the results achieved under the program, I am somewhat concerned about the high rate of inflation, which has eroded part of the depreciation of the dalasi. I therefore wonder whether the projections set for 1987/88 are not a little on the optimistic side. I would encourage the authorities to monitor developments very carefully.

Third, regarding the current account deficit, I am somewhat puzzled by the slow pace of reduction forecast for the next five years. Although I recognize that this relatively slow pace of adjustment is sustainable in light of the high level of transfers from the international community, I think that this objective should be more ambitious, especially since a large part of The Gambia's exports are in fact re-exports to neighboring countries. The level of these re-exports could be substantially and rapidly reduced in the future if customs enforcement was strengthened or import tariffs reduced.

Mr. Iljas made the following statement:

I am in broad agreement with the staff appraisal. I commend the Gambian authorities for their timely and firm implementation of various structural reforms under the structural adjustment arrangement, as well as for their adherence to adjustment efforts under the stand-by arrangement. These measures have helped improve the performance of the economy and helped elicit substantial financial support from the international community.

Despite the favorable developments, the economy remains vulnerable. Inflation, although decreasing, is still relatively high, while the external and fiscal positions are highly dependent on official transfers and concessional lending. I therefore welcome the authorities' commitment to continue their efforts to strengthen policies already in place, while pursuing measures outlined in the policy framework paper to expand production, improve public sector management, and rationalize exchange rate and other pricing policies.

> I support the introduction of various policies to enhance production, especially in the agricultural sector. The rationalization of the groundnut subsector and the reform in the agricultural credit system, for instance, will help stimulate agricultural production. In this regard, I am pleased to note that the recent improvement in the agricultural sector has increased employment opportunities and has helped absorb some of the workers laid off as a result of the Government's program of retrenchment in the civil service.
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> It is also of particular importance to continue reducing the budgetary deficit. In this respect, I welcome the introduction of a general sales tax, income tax reform, and measures to strengthen tax administration. Together with continued expenditure restraint, the elimination of subsidies, and the rationalization of public enterprises, these efforts will help improve fiscal performance in the medium term.
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> Finally, I welcome the authorities' continued efforts to promote efficient resource allocation by maintaining flexible exchange and interest rate policies, and rationalizing petroleum and public utility prices. I support the proposed decisions.

Mr. Goos stated that he was impressed by the recent economic performance of The Gambia, which could be traced clearly to the authorities' commendable adjustment policies. The progress with respect to inflation, the strong recovery in domestic economic activity, and the turnaround in private capital flows were noteworthy achievements. The latter development was evidence of renewed confidence in the authorities' policy stance, but as such flows were highly sensitive to shifts in policy orientation, close adherence to the adjustment course agreed under the policy framework paper would be of paramount importance. Most of the improvement in the external capital account had been devoted to a greater than anticipated increase in external reserves, a not inappropriate course. However, the effect of the increase in external reserves in bolstering private sector confidence might have been partially offset by the relaxation of the current account target and the upward revision in the growth target. Although he appreciated the authorities' desire to aim at higher per capita income levels, the precarious external payments situation suggested that the highest priorities should be the restoration of a viable current account position, and a reduction in payments arrears. As the normalization of relations with creditors was of crucial importance, the authorities might consider relaxing their external reserve target, thus creating additional scope for the quick settlement of existing payments arrears.

Monetary policy, like fiscal policy, would continue to be vital in stabilizing domestic and external developments, Mr. Goos continued. He had noted with approval the authorities' intention to maintain a flexible interest rate policy, so as to counter possible pressures on domestic prices and the foreign exchange market. However, he was concerned that the substantial slippages in the monetary target for the year might have created dangerous inflationary pressures. While such pressures might be difficult to gauge in view of the possible further financial deepening of the economy, monetary developments should be monitored very closely, so that excess liquidity that might lead to compromising the inflation target would be quickly absorbed.

Finally, in view of the Gambian economy's narrow productive base, it might be appropriate to intensify efforts to provide direct incentives to private sector activity in new production, Mr. Goos concluded, especially in production with promising export potential. He endorsed the staff appraisal and supported the proposed decisions.

Mr. Al-Assaf made the following statement:

It is encouraging to note that The Gambia has been making some significant progress under the first year of the structural adjustment arrangement and the stand-by arrangement approved last year. I therefore commend the authorities for their efforts. Clearly, more will need to be done, as The Gambia continues to face very serious economic and financial problems.

The magnitude of the imbalances still present in the economy--domestic and external--are reason for caution in the longer term. External debt, expressed in terms of GDP, is not expected to decline from its present extremely high level during the course of the program. The servicing of the external debt will therefore continue to absorb a large proportion of available external sources of financing. Also, the large size of the budget deficit will require determined efforts on the revenue as well as on the expenditure side, if the objectives of the three-year program are to be achieved.

With these preoccupations in mind, I would like to make the following points on some aspects of the 1987/88 program.

On the domestic side, the authorities intend to pursue their efforts to simplify the structure of the tax system and improve the degree of elasticity of indirect taxes. This is clearly a move in the right direction, especially in view of the authorities' revenue objectives for the years ahead. It is noteworthy, however, that two of the most significant changes contemplated over the period of the 1987-88 program, namely, the reform of the income tax and the introduction of a sales tax, will not be implemented until the latter part of the financial year. Therefore, the positive effects of these changes will not be seen until the 1988/89 arrangement has been well under way. From a longer-term perspective, however, these are very positive changes that should help reduce tax evasion and dependence on official external transactions as a source of revenue.

On the external side, I have noted that the current account deficit reduction has not been proceeding at the expected rate. In view of the need to maintain a level of imports consistent with the achievement of at least a modest rate of economic growth, the key to a significant improvement seems to be in the promotion of exports. The program does not envisage that exports can reasonably be expected to expand at a rapid rate, and I assume that this reflects the structural constraints faced by the country. This would seem to indicate that significant progress on the external side, in the long run, will crucially depend on a successful diversification of the export base. Of course, this is not an area where the Fund can take a leading role, but I hope that the World Bank will find it possible to develop its activities in The Gambia in this regard.

Finally, I would like to commend the authorities for addressing in a decisive way the issue of government transfers to parastatals and, in particular, the difficult issue of the financial balance of the Gambia Produce Marketing Board (GPMB). In the 1987/88 program, this will involve a large one-time transfer to the GPMB equivalent to 8 percent of GDP. I am unsure, however, about the medium-term effects of the reform of the GPMB and the ways in which a recurrence of the present financial difficulties might be prevented in the future. I have noted in particular that a key element of the turnaround in the accounts of the GPMB is a further decline in producer prices, on top of a previous reduction of 17 percent implemented this calendar year. While such cuts may have immediate beneficial effects on the accounts of the GPMB, it is not certain that they represent a viable long-term solution. More important, they may have direct implications for the balance of payments and the development of recorded exports. I also wonder whether further adjustments in producer prices would be consistent with the objectives of the 1985 Economic Recovery Program. One of those objectives was to reduce the divergence between urban and rural standards of living. Some progress has been achieved in this direction, but further cuts in producer prices could affect these achievements, and I would be interested to know if this factor is being taken into account for the future. I support the proposed decisions.

Mrs. Walker made the following statement:

We commend the Gambian authorities for their consistent pursuit of adjustment policies under the Economic Recovery Program supported by the Fund, and welcome the fact that the authorities have continued to carry out reforms under this program since the first year of the structural adjustment arrangement ended in July 1987. It is unfortunate that it has taken so long to bring the revised policy framework paper to the Board for approval of the second year of the structural adjustment arrangement, which I understand still conforms to the fiscal year, but we understand the timing constraints that have contributed to this situation, which we hope could remain an exception and not the rule. We also agree that the best way to proceed at this time is with a structural adjustment facility program only, particularly in light of The Gambia's need for concessional assistance.

Several elements of the adjustment program are of particular importance to the overall success of the adjustment effort. We welcome the authorities' efforts to encourage more private sector activity in the economy, including the restrictions on the Ministry of Agriculture's activities, the divestiture program, and the revised investment code. The reduction of subsidies to the groundnut sector, including the virtual elimination of the subsidy to the Gambia Produce Marketing Board by 1989/90, and the relative changes in producer prices to align them more closely with world prices, are positive developments which should contribute to improvements in the Government's fiscal position. The civil service retrenchment, which was assuredly a difficult process, as well as the decision not to grant a salary increase, will contribute to a more sustainable fiscal situation. The maintenance of a flexible exchange rate policy has been critical to the overall success of the adjustment program thus far, and we commend the authorities for adhering to it. The pass-through of pricing changes to consumers has been successful, although we would prefer a somewhat more flexible pricing approach. The more flexible interest rate policy, which has achieved positive real rates, should also be continued.

The adoption and maintenance of the adjustment program has enabled The Gambia to receive significant exceptional assistance. While we are troubled that the narrowing of the current account deficit will not be as great as originally expected, it is noteworthy that reserve accumulation will be more adequate and that arrears have been reduced more than expected. Restoration of normal debtor-creditor relations is clearly important to ensuring that adequate amounts of external assistance will be available in the future.

Since the above-mentioned policies have been carried out throughout the second year of the structural adjustment arrangement, even though the revised policy framework paper had not been formally discussed, we expect that these measures will be continued through the remainder of the year. Specifically, the attainment of the objectives for this program year will depend on strict maintenance of the agreed fiscal and groundnut producer pricing measures. In addition, we anticipate enactment of the investment code and of the agricultural reform, and continuation of the public divestiture program and the signing of contracts with remaining enterprises. In next year's program, we expect implementation of additional measures to diversify The Gambia's exports in the fisheries and tourism sectors, as well as further measures to expand the agricultural sector, including horticulture. Finally, we are convinced that reaching balance of payments viability in The Gambia should remain a key goal of the structural adjustment program.

The Gambia's economy is clearly improving although its restructuring is difficult and much remains to be done. In spite of the constraints inherent in a small and poor economy, and the limited technical expertise available to administer the adjustment program, The Gambia has made remarkable progress, and we encourage the authorities to continue their program.

Mr. Othman stated that the Gambian case was a good example of how countries could benefit from the international community's financial support in realizing their main objective of adjustment with growth. It was also a good example of how the appropriate adjustment measures could elicit a high level of financial support from the international community. The Gambia's economic performance was commendable, as reflected in the successful implementation of the 1986/87 program, especially the impressive rate of growth in real GDP of 6 percent, compared with a target of 3.3 percent.

As he was in broad agreement with the staff, Mr. Othman said, he would confine himself to the following brief remarks. The authorities were to be commended for their success in implementing the retrenchment program in the public sector, the 20 percent reduction in public sector employment being particularly remarkable. The relatively high rate of growth in 1986-87 had probably helped the private sector to absorb part of that labor force. Some elaboration by the staff on how the economy reacted to such a substantial reduction in public sector employment would be helpful.

The Gambia's prudent management of its foreign debt, reflected in the timely servicing of its debt, including its obligations to the Fund, was notable, Mr. Othman went on. However, in spite of recent improvements the balance of payments remained vulnerable. Therefore, continued international financial support was essential to enable the Gambian authorities to retain the gains that had already been made, and to strengthen the momentum and pace of adjustment in the direction of establishing a solid basis for durable economic growth and a viable balance of payments.

Given the traditional marked disparity between urban and rural standards of living, the improvement in rural income that occurred since 1985/86 was most welcome, Mr. Othman remarked. That improvement was apparently due to a rise in producer prices and expansion in production of groundnuts. In 1987, however, producer prices were reduced by 17 percent, which brought them closer to international prices. While his chair fully endorsed the authorities' move to align producer prices with international levels, thus also helping the fiscal position, the effect of such a sharp reduction in producer prices on income distribution bore scrutiny. He supported the proposed decisions.

Mr. Hammoudi made the following statement:

Since the Gambian authorities are in broad agreement with the conclusions of the staff appraisal, I have few remarks to make. I support the proposed decisions.

The authorities are to be commended for the progress made since mid-1985, when the three-year Economic Recovery Program (ERP) was initiated. The first-year results achieved by The Gambia are encouraging, as the growth in GDP is now estimated at about 6 percent, compared with the target of 3.3 percent, and the inflation rate has declined to about 20 percent, from 70 percent in 1985/86. While a slippage has occurred in the fiscal deficit, which is estimated at about 21.3 percent of GDP, compared with the target of 17.5 percent, the Government's net position vis-à-vis the banking system has turned positive, and the overall balance of payments deficit (excluding exceptional financing), which was projected at about SDR 20.4 million, has reached equilibrium level.

These achievements are due to the Gambian authorities' implementation of structural policy measures aimed at removing the imbalances and financial difficulties they had encountered before the initiation of the Economic Recovery Program. All the benchmarks on structural policy measures were met with respect to the investment code, civil service reform, public investment, public enterprises, and fiscal policy. Moreover, I welcome the Gambian authorities' stated willingness to take further action in 1987/88 to accelerate the pace of the adjustment program, in particular, to reduce the fiscal deficit through expenditure restraint; to improve the system of tax collection; to strengthen the monetary and credit program; to contain the external current account deficit; to liberalize the domestic groundnut market; to reform the agricultural credit system; and to reinforce the private sector, especially with respect to agricultural trade, fisheries, and tourism, which would have the effect of increasing government foreign exchange earnings.

I would like to make two specific remarks on the financial situation of GPMB and the improvement in rural incomes. First, I wonder how the GPMB could possibly repay its debt to the Central Bank, which is estimated at almost 8 percent of the country's GDP, and at the same time balance its financial situation, at a time when the Government is required to sharply reduce the groundnut subsidy element by 4 percent. What is even worse, while losing its monopolistic position, the GPMB has to face a decline in the price for groundnuts of about 16.7 percent for the 1987/88 crop season, and a level of groundnut production which is lower than expected. Second, I see some contradiction in the staff report when I read about an increase in rural incomes on the one hand, and about a fall in groundnut prices by about 16.7 percent, which constitutes the main revenue for the rural population, on the other hand. I am thus somewhat concerned about the negative social impact of these issues, as well as of the increase in prices of basic commodities and services, and the large number of job losses. It would be helpful to have the staff's comments on these issues.

The staff representative from the African Department explained that the slippage in bringing the paper on the second annual structural adjustment arrangement to the Board was due chiefly to the fact that two formal reviews under the previous stand-by arrangement had had to be completed, as the authorities had noted in the letter of intent. The second review was to have been completed by September 15, 1987, and in fact had been brought to the Board along with the Article IV consultation on August 31. The staff had subsequently visited The Gambia and concluded discussions with the Gambian authorities during the Annual Meetings. Given the usual lags, the papers were completed in mid-November. Another factor contributing to the delay was the need for verification of compliance with the performance criteria for end-June 1987 under the stand-by arrangement. The data base and the administrative machinery were often rather weak in low-income countries, and time had been needed following the end of the fiscal year on June 30 to verify performance and to set a firm base for making projections for the new structural adjustment program. However, the staff could shorten the lag next year, especially as there would be no formal review process associated with the current structural adjustment arrangement. Nevertheless, to allow time for performance verification, a lag of some six to eight weeks after the end of the fiscal year might be expected, implying that the report to the Board could be made by September or, more probably, by October. In any case, a shortening of the lag by about two months would be possible.

With respect to program design, the staff representative continued, several Directors had asked about the implications for rural incomes of the reduced producer price for groundnuts, and whether it was consistent with the Economic Recovery Program adopted in 1985, which had sought to promote rural incomes. There had been a very large increase in producer prices over the period 1984-86, on the order of 60 percent, and the recent reduction in the domestic producer price of 17 percent had not offset the increase in prices over the previous period. The policy framework paper had also explained that an increase in the production of other crops might compensate to a certain extent for the decrease in the domestic producer price for groundnuts. Finally, the program was premised on the maintenance of cross-border flows to the neighboring country, as the price there, even though it might come down, was likely to remain higher than in The Gambia. These flows might not be on the same level as in 1987/88, but they would still be important.

The slippage in the fiscal deficit from the target of 17.5 percent to 21.5 percent of GDP in 1986/87 was more apparent than real, the staff representative went on, in that the Government had taken over some non-performing assets of The Gambia Commercial and Development Bank through implementation of the Managed Fund; otherwise, the deficit would have been only 14.4 percent of GDP. Concerning the impact on the fiscal position, of the large transfer to the GPMB in 1987/88, the negative effects would be offset by measures to restrain expenditures and to increase revenues, as well as by the significant amount of foreign financing that was expected. These factors would allow The Gambia not only to meet the budgetary target, but also to increase the Government's net creditor position with the banking system. With respect to the collection of tax arrears of the public enterprises, in view of the re-estimation of the arrears at a much lower level, namely, D 1.6 million, and the limited tax administration capability in The Gambia, the authorities had not accorded the matter a high priority.

Although inflation had been at a very high 70 percent in the period 1985/86, at the time of the depreciation of the currency, the staff representative recalled, it had subsequently fallen in the succeeding 12 months to a rate of 20 percent, and over the first 7 months of 1987 to about 12 percent. Consequently, the 12.5 percent target rate for 1987/88 appeared feasible.

With respect to the possibility of accelerating the timetable for the elimination of the external arrears, the authorities had made a courageous commitment to eliminate the arrears by the end of the current three-year period, something which had not been anticipated at the inception of the first structural adjustment arrangement, the staff representative from the African Department concluded. Their commitment had already increased confidence among creditors, as was evidenced by the larger than anticipated amount of official assistance which had been forthcoming. The authorities had also attached a high priority to maintaining a minimum level of reserves. That being said, an accelerated rate of arrears elimination did not appear necessary.

The Executive Board then took the following decisions:

Structural Adjustment Facility - Second Annual Arrangement

1. The Government of The Gambia has requested the second annual arrangement under the structural adjustment facility.

2. The Fund has appraised the progress of The Gambia in implementing the policies and reaching the objectives of the program supported by the first annual arrangement, and notes the updated policy framework paper (EBD/87/300).

3. The Fund approves the arrangement set forth in EBS/87/236, Supplement 1.

Decision No. 8762-(87/179), adopted
December 23, 1987

Exchange System

The Fund grants approval for the retention by The Gambia of the exchange restrictions evidenced by external payments arrears and of the exchange restrictions remaining pending the execution of the rescheduling agreements with each individual creditor until August 31, 1988, or the next Article IV consultation with The Gambia, whichever is earlier.

Decision No. 8763-(87/179), adopted
December 23, 1987

## 2. COLOMBIA - 1987 ARTICLE IV CONSULTATION AND RELEASE OF INFORMATION

The Executive Directors considered the staff report for the 1987 Article IV consultation with Colombia (SM/87/278, 11/24/87; and Cor. 1, 12/11/87). They also had before them a background paper on recent economic developments in Colombia (SM/87/285, 12/7/87).

Mr. Kafka made the following statement:

My authorities are in general agreement with the thrust of the staff report for the 1987 Article IV consultation, and we can endorse the proposed decisions. Nevertheless, my authorities wish to emphasize certain aspects of key policy actions taken in the most recent years.

Although there was a formal monitoring of the Colombian program by the Fund during 1985-86, this year the creditor banks did not insist on a formal monitoring exercise, as Colombia has made decisive progress toward re-establishing internal and external equilibrium. For 1987-88, the authorities have agreed to deliver copies of the Fund Article IV consultation reports to creditor banks, if the Board agrees.

During 1987, for the fourth consecutive year, Colombia achieved an important rate of economic growth accompanied recently by a moderate inflation rate. The current account deficit of the balance of payments was only 1 percent of GDP. At the end of 1987, gross international reserves had recovered to the equivalent of 11 months of merchandise imports, compared with 5 months at the end of 1984. The authorities are determined to continue to pursue a strong growth-oriented strategy in order to offset the serious setback which took place during the 1981-83 recession, and they will continue their efforts to lower the rate of unemployment, which at the end of 1987 was approximately 11 percent.

The performance of the Colombian economy was indeed commendable, especially in view of the politically important and difficult adjustments and reforms the authorities had to implement. Colombia's 1984-86 economic recovery was significantly assisted by the sharp increase in coffee export prices (related to the 1986 frost in Brazil), and by the coming on stream of the very important petroleum and coal projects and their concomitant exports. It is also noteworthy that other nontraditional exports rose 21 percent in dollar value over the 12-month period from November 1986 to November 1987. The authorities' timely actions to sterilize the large revenue increase arising from coffee, petroleum, and coal exports in 1986 and 1987 in order to prevent an excessive growth of aggregate demand deserve particular mention. The Banco de la República intensified its over-the-counter operations, issuing paper of various maturities (from eight days to six months), and prudent amounts of U.S. dollar-denominated bonds.

The cornerstones of the successful recovery of the Colombian economy were expenditure restraint, a prudent policy with respect to foreign indebtedness, and a flexible exchange rate policy. Fiscal and trade reforms also played important roles.

The tax reforms were aimed at stimulating personal savings and equity investment. The authorities therefore unified the corporate income tax rate, lowered personal income tax rates, broadened the income tax base, and eliminated the double taxation of dividends and the deductions of interest payments by corporations. National savings rose to approximately 17 percent of GDP in 1986-87, compared with 12 percent in 1983-85, as a result of higher coffee prices.

On monetary policy, the management of the interest rate deserves special mention. The authorities observed that due to market imperfections, market-determined interest rates were high in real terms, and "sticky" to downward movements. At the beginning of 1986 the authorities lowered the interest rate, by decree, by 4 percentage points. Six months later, the decree was abolished and interest rates continued to decline. Government regulation thus pushed the private sector to act appropriately--a lesson for the Fund as well as for other countries.

The authorities also made substantial progress in liberalizing trade. As reported by the staff, prior import licensing now applies mainly to nonessential consumer goods, and there was a significant reduction in the degree of dispersion of tariff rates and in the average level of effective protection. Similarly, foreign direct investment policies were substantially liberalized, and draft legislation to permit new foreign investment in the financial sector was submitted to Congress.

Colombia will continue to administer its exchange system flexibly, with a view to external competitiveness. Given the history of unstable prices of traditional export products over the last 25 years and the consequent variability of export revenues, my authorities stress that it is necessary for Colombia to maintain control over foreign exchange, via the monetary authority. Management and control of such a scarce and, at times, volatile resource provides stability guarding against a lack of confidence, and/or speculative attitudes which invariably arise during periods of cyclical downturns in the external sector. My authorities believe that in periods of cyclical downturn the free movement of exchange rates could lead to harmful instability. Certain controls and regulations which moderate fluctuations and deter speculation are, therefore, helpful in such situations.

Another good reason for maintaining control over the foreign exchange system in the case of Colombia is the authorities' desire to prevent excessive foreign indebtedness of the public and/or private sectors, and the capacity such control provides for rejecting foreign loans with excessive financial costs and short-term maturities.

Colombia has traditionally maintained a conservative approach to commercial bank indebtedness. As a result, an unusually high proportion of the debt outstanding at the end of 1987 (US$12.1 billion) was owed to multilateral development financing institutions. Debt service in relation to exports of goods and services reached 47 percent in 1987. The high debt service ratio is due to the fact that exports of goods and services are not particularly large in relation to GDP (18 percent), and because Colombia has never renegotiated its foreign debt with the banks or with Paris Club members. Colombia faces heavy amortization payments over the period 1988-90 but expects to be able to finance the principal payments without difficulty.

The medium-term scenario presented by the staff seems attainable under appropriate and realistic policies. The authorities will aim for an annual growth rate of 5 percent an equilibrium in the balance of payments. If the targets are reached, the foreign debt/GDP ratio would decline from 44 percent in 1987 to 31 percent in 1992, and the debt service ratio would be reduced by 13 percentage points, to 34 percent of exports, by 1992. However, it is borne in mind that a decline of US$1 in the price of petroleum, of US$0.10 in the price of coffee, and an increase of 1 percent in the rate of interest paid on external obligations would have the effect of widening the annual current account deficit from 1.5 to 2.4 percent of GDP; and, therefore, the annual financing gap during the period would be approximately US$430 million. Correspondingly, in 1992, the foreign debt/GDP ratio would jump to 35 percent from the projected 31 percent, while the debt service ratio would exceed 38 percent, compared with the projected 34 percent. Hence, the importance of a favorable external economic environment for Colombia cannot be overemphasized.

Colombia has done exceptionally well in the difficult year that is about to end and is well placed to sustain a significant rate of growth in the context of a sound balance of payments, with further progress toward stabilization.

With regard to certain statistical reporting issues raised in Attachment II of the staff report, my authorities feel that they are reporting appropriately, and have agreed to a technical visit from the Bureau of Statistics to study the matter and resolve any issues that arise.

Mr. Feldman made the following statement:

The staff is to be commended for its comprehensive analysis, as well as for the complete statistical information on Colombian economic performance.

As Mr. Kafka points out in his illustrative statement, Colombia has undoubtedly carried out significant external and internal adjustment in 1985-86, founded on a tightening of demand policies and a significant depreciation of the domestic currency in real effective terms. As a consequence of these policies, domestic savings increased while investment declined, and the current account of the balance of payments showed a dramatic turnaround, from a deficit of 10 percent of GDP in 1982-83 to a surplus of 2 percent of GDP in 1986.

During 1985 and especially during 1986, Colombia's strong adjustment effort took place under a favorable external condition--the international price of coffee rose sharply, thus boosting the country's export and fiscal revenues. Colombia's experience with this favorable exogenous circumstance contrasts sharply with that of other Latin American indebted countries, which had embarked on adjustment programs but in an adverse external environment. This favorable external situation allowed Colombia to achieve a growth of GDP of 5 percent during 1986 and 1987, meaning that the country's rate of economic growth recovered to that of the late 1970s. Colombia achieved these results with a remarkably stable and, by Latin American standards, relatively low rate of inflation, and with a level of foreign indebtedness that, so far, has proved to be manageable.

The adjustment of the Colombian economy actually started in 1982. Colombia's adjustment was at first basically internal, since emphasis was not placed on the correction of external imbalances until after 1985. This is again in contrast with other Latin American countries, where foreign indebtedness was the key obstacle to the attainment of internal and external balance, and hence resort to voluntary lending from commercial banks was not possible. From 1982 the fiscal situation in Colombia improved practically without interruption, with total expenditures remaining remarkably stable and total revenues increasing steadily, by 8 percentage points of GDP between 1982 and 1986. A successful tax reform coupled with the higher operating surplus of public enterprises (notably the National Coffee Fund) explain these positive results. On the external side, import restrictions bore the burden of correcting Colombia's trade imbalances until 1985.

The economic adjustment initiated in 1982 and furthered in 1985-86 was not without costs. Economic activity during the years 1982 through 1985 slowed to an average growth rate of 2 percent per annum, a rate that is slightly above the rate of population growth. That economic performance, however, did not provide for the absorption into the labor market of the annual increase in the labor supply in Colombia; consequently, the rate of unemployment increased from about 9 percent in 1982 to over 14 percent in the first half of 1986, declining only a little in the last year and a half. The low rate of growth, presumably combined with the development of highly capital-intensive investment projects, led to a very weak demand for labor, a matter which certainly must concern the Colombian authorities in their future growth strategy. In this respect, during 1982-86, unit labor costs in Colombia fell by more than 30 percent in real terms, while the gap between labor productivity and real wages in manufacturing widened by about 20 percent. This trend allowed for an increase in firms' profitability and helps to explain the private sector's increasing reliance on self-financing, a feature pointed out in the staff report.

In contrast with 1986, 1987 has been a difficult year for the Colombian economy, given the unfavorable external shock resulting from the sharp decline in the international price of coffee. Such an adverse circumstance has negatively affected both the fiscal and the external accounts of Colombia, although fortunately within manageable limits. We fully share Mr. Kafka's assessment that Colombia has done exceptionally well in this difficult year. The Colombian authorities are to be praised for their prudent monetary and fiscal policies as well as for the consistency of their exchange rate policies. Since 1982 the Colombian peso has depreciated by about 50 percent, with most of the adjustment being carried out since 1985. This drastic change in relative prices has allowed Colombia to diversify and enlarge its export base; in fact, the level of exports for the biennium 1986-87 will be on average more than 50 percent higher than the level of the four preceding years. In our view, the soundness of Colombia's external policies will offset most of the damaging effect on the external accounts resulting from the decline in the price of coffee.

With respect to the medium-term outlook, we feel that the staff projections are realistic but rather on the cautious side, since the Colombian economy has shown itself to be very sensitive to export incentives. In particular, the development of mineral resources and the dramatic growth of nontraditional exports are grounds for expecting a reasonable external situation consistent with the targeted rate of real economic growth. Notwithstanding its recent successful performance, Colombia may remain quite vulnerable to adverse shocks for a rather long period, and the continuous implementation of consistent demand-management and structural policies to minimize their impact will be crucial. A key factor in the Colombian economic outlook is the role of the international financial community in supporting the country's adjustment efforts. It is hard to understand the commercial banks' delays in completing the Colombian financial package. Colombia is a relatively "noncrucial" case among the indebted nations, the debt burden is more manageable than that of the big Latin American debtors, and still the banks have not started disbursements, thus increasing the uncertainty of Colombia's economic prospects. Perhaps the staff has more information on this and would like to make some additional comments.

While we agree that Colombia's recent economic improvement has been remarkable, and that its external competitiveness is appropriate at present, we do not share the staff's view that the exchange rate must bear the burden of any eventual external shock. In our view, if Colombia must face unexpected movements in international prices or interest rates, it should do so with the help of additional external financing, and not via additional internal adjustment.

The central question for the Colombian economy in the medium term is the need to reinvigorate the process of private investment. Fixed capital formation by the private sector has been declining in recent years; it seems of utmost importance that this trend be reversed, in order to achieve sustained growth and a lower unemployment rate, the latter of which may be a distressing source of political and social instability. In our view, the resumption of private investment requires the gradual reduction of inflation and of real interest rates. We think that Colombia is in the best position to achieve these objectives, so long as the authorities persist with consistent macroeconomic policies combined with a cautious liberalization of foreign trade. We fully agree with Mr. Kafka that it is necessary for a country like Colombia to maintain certain controls and regulations on the functioning of the foreign exchange market. Demand-management policies and, in particular, fiscal policy, should allow for the necessary reduction in real lending rates and in the rate of inflation. More important, the authorities should refrain from further depreciating the Colombian peso if a gradual deceleration of inflation is sought. After all, between early 1982 and mid-1984 the rate of inflation fell from 25 percent to 15 percent per annum, and the subsequent reacceleration to the present rate has been the cost, albeit a reasonable one, for achieving a dramatic improvement in Colombia's external competitiveness.

We support the proposed decisions.

Mr. Noriega made the following statement:

On the basis of some preliminary indicators for 1987 one may conclude that the Colombian economy maintains its growth momentum along with overall financial stability. This is indeed a commendable achievement, made even more so because it is the outcome of a very prudent policy stance. In fact, instead of aiming for even faster growth in the short run by taking advantage of favorable developments in the external environment, the authorities have opted to introduce difficult adjustment and reforms, which will probably lead to more permanent enhancement of future growth prospects.

We are in broad agreement with the staff's appraisal of the past evolution of the economy, and considering the Government's prudent approach as explained in Mr. Kafka's statement, we feel assured with respect to the short- and medium-term prospects. This assurance, however, should not distract us from the fact that the economy remains vulnerable to external shocks, that unemployment continues unabated, and that inflation has not been eliminated.

Nevertheless, the remarkable progress in correcting the internal and external imbalances and in raising the rate of income growth during the last three years puts Colombia in a privileged position. With no urgent needs requiring prompt action, the Government can devote itself to studying different alternatives for overcoming the more chronic problems. We endorse the thrust of current policies, and my comments should be taken in this vein.

With respect to the fiscal sector, we note that the Colombian authorities took full advantage of the favorable external conditions that prevailed in 1986-87 to implement significant changes in tax legislation. Thus, the Central Government's financial situation has further improved in 1987, notwithstanding the reduction of several tax rates prescribed by the tax reform approved in late 1986, and the revenue loss stemming from lower coffee prices. However, the increased relative importance of fiscal revenues accruing from international trade will continue to expose public finances to external shocks. Thus, a shift toward greater reliance on revenue from domestic income should provide an automatic stabilizer to the economy.

On the expenditure side, external interest payments have become important, although they are still at a moderate level. It would therefore be advisable for the authorities to remain cautious in contracting foreign debt. The liberalization of foreign investment regulations is a positive step in this direction.

Regarding the financial sector, the most puzzling issue is the relatively high rate of inflation, currently at 24 percent. The comment by the staff that "a floor of about 20 percent seems to have developed in practice" and that wage indexation is one of the main causes of inflation is not a satisfactory explanation. The main ingredients for a stabilization policy seem to have been effected: compression of the fiscal deficit, restrained credit expansion, substantial trade liberalization, and a successful reduction of interest rates. Furthermore, private holdings of financial assets continue to grow in real terms, and the central bank has accumulated international reserves. Excessive demand, therefore, does not appear to be causing inflation. Nor do the authorities feel that the determination of public and minimum wages has a major impact on other private wages; therefore, this cost element would not be responsible for inflation either. The tables in the statistical appendix to the background paper on recent economic developments show that real wages have remained relatively constant since early 1984. We would be interested to hear the staff's views on the indexation scheme, and on the effects of the real depreciation of the exchange rate on current inflation.

We have some reservations regarding the medium-term scenarios presented in the staff report. There was a very significant increase of 15 percent in nontraditional exports in 1987. However, this was due partly to the real depreciation of the exchange rate, which may not be repeated, yet the level of nontraditional exports is assumed to grow at a rate of more than 13 percent annually through 1992. For the same reason, the mean rate of growth of imports, of more than 10 percent annually, seems somewhat optimistic. As the Government has concluded major investment projects, and as it intends to emphasize social investments which traditionally have a large component of domestic inputs, the assumed increase in imports would be mainly at the impulse of the private sector; thus, a somewhat slower growth could be more realistic. In this scenario, international reserves as a proportion of merchandise imports fall, and although my previous comments should make me more optimistic about the eventual outcome for this ratio, I wonder whether this target is adequate or not. The good record of debt servicing would lead us to expect that the country may rely increasingly on borrowed reserves as a substitute for its own reserves. However, more difficulties were encountered in concluding the financing package with the commercial banks than initially expected. Therefore, a moderate increase in reserves may be warranted under these circumstances. In this connection, like Mr. Feldman, I would appreciate it if the staff could indicate the state of the negotiations with commercial banks, and the reasons for the delay in disbursement.

I wish to reiterate our recognition of the Colombian authorities' consistent economic policy. We support the proposed decisions.

Mr. Enoch made the following statement:

I fully share the views expressed in the staff appraisal. The Colombian authorities have maintained a consistent and prudent macroeconomic policy stance over the last few years; they are now reaping the benefits. They are closer than just about any other Latin American country to restoring normal relations with their external creditors. Colombia's general performance under the 1985-86 program of enhanced monitoring, and during 1987, demonstrates the compatibility of economic growth with adjustment.

Colombia's prudent policies have been maintained over the last year. While there was a significant deterioration in the fiscal balance, I recognize that this was essentially due to the fall in the international coffee price and to higher interest payments on domestic and external debt. I can welcome the shift in expenditure toward investment in social sectors, which should help to improve living standards. However, the surge in income tax receipts owing to the tax amnesty is a one-time phenomenon, and some additional fiscal restraint will be necessary to make up for it in 1988. As the staff notes, a cautious expenditure policy remains appropriate, and pressures for increased expenditure should be resisted.

Monetary policy has also been effectively and successfully managed, and fully supported by the fiscal stance. The very sizable increase in gross national savings is noteworthy. The increase in reserve requirements and the use of open market operations in 1987 helped to control domestic credit, and the increased market orientation of interest rates on funds managed by the Banco de la República is very welcome.

Previous speakers have already alluded to the problem of inflation. While inflation is relatively low by regional standards, it has persisted for many years and is by no means insignificant. While it persists there is always a risk it may get out of hand. As the staff notes, its elimination could contribute to sustainable growth. The continuation of sound fiscal and monetary policies should help in this respect, but the current wage indexation arrangements seem to be a significant obstacle. I would welcome comments on this last point. A shift to more forward-looking indexation would be very helpful, although I realize that the authorities' scope for action here is limited by legal constraints.

Further opening of the economy might have a number of benefits, including helping to reduce inflation further, although we recognize that the external position represents something of a constraint in this regard. The balance of payments projections generally look very favorable, but they are inevitably very vulnerable to international interest rates, to coffee prices and, increasingly, to oil prices. It is therefore important that further liberalization be accompanied by the continuation of the present flexible exchange rate strategy, so as to be able to offset any negative impact on the balance of payments. I note that the current official exchange rate is very close to the unofficial rate, and would associate it with a strong performance in nontraditional exports. The present level of reserves looks healthy, and a reflection of the past success of the authorities' policies. I welcome the easing of import controls in June 1987. The liberalization of foreign direct investment is also very welcome, and I would join with the staff in urging the authorities to extend this liberalization process to other exchange restrictions and multiple currency practices. In this connection, I wonder whether the staff has a role in assisting the authorities in planning a timetable for the reduction of restrictions and the elimination of multiple currency practices.

In conclusion, I would like to commend the authorities for maintaining the very sound record of economic policy which they have established over the last few years. I support the proposed decision and the authorities' request for the staff reports to be released to their creditor banks and other financial institutions, representing a reduced level of Fund involvement from the program of enhanced monitoring that is to be welcomed as evidence of progress.

Mr. Goos made the following statement:

In general, I share the view that the authorities have continued to pursue quite judicious economic and financial policies this year, and I am pleased to note their intention to adhere to a cautious policy stance in the years ahead as well. I think it is worth emphasizing that the continued adjustment efforts of the recent past are now paying off, as reflected in the impressive growth performance, in the considerable strengthening in the external position and, above all, in the expected resumption of substantial lending by commercial banks on largely voluntary terms. I believe Colombia is the first Latin American debtor country to which the banks have resumed voluntary lending since the outbreak of the debt crisis. This experience is clearly exemplary, and notwithstanding its special characteristics, as emphasized by Mr. Feldman, I think it should provide important lessons to other highly indebted countries.

Nevertheless, the staff rightly points to several policy areas that require the authorities' continued and, in some cases, increased attention. First, as has been stressed by previous speakers, it is clear that prudent financial policies will remain crucial for a satisfactory domestic and external performance, particularly in view of the vulnerability of the balance of payments to external shocks. This vulnerability has again been highlighted by the recent decline in oil prices, and one wonders whether the authorities should not aim at a more ambitious fiscal deficit target for 1988 than that of merely trying to keep the deficit constant in terms of GDP. The creation of a safety margin in the fiscal position against unexpected external developments could also help reduce the pressure on domestic prices, and thereby make an important contribution to further strengthening private sector confidence and investment. Moreover, further progress in fiscal adjustment would also be advisable in order to contain public sector debt and, in particular, foreign borrowing.

In this context, I am concerned that the authorities' approach to domestic price stabilization might be too gradual. While gains in labor productivity could help to alleviate the problem, I am afraid that the necessary expansion of investment in industrial capacity could further fuel inflationary pressures by increasing demand in the domestic manufacturing sector which, according to the authorities, is already operating near full capacity. Accordingly, I would agree with the staff and previous speakers that, in addition to the need for maintaining sufficiently restrictive financial policies, domestic price stabilization should be pursued simultaneously, first by delinking wage indexation from past inflation, and second, by accelerating the pace of liberalization of exchange and trade restrictions so as to improve the domestic supply situation. Moreover, the authorities should make an effort to phase out central bank financing of the fiscal deficits, and aim to accelerate the reform of the financial system with a view to further strengthening the incentives for the mobilization of savings and an efficient allocation of resources. While important progress has already been made in liberalizing the economy, the staff report gives clear evidence that more needs to be done in order to enhance private sector initiative, including the inflow of foreign direct investment, and to improve overall efficiency.

Although I had intended to support the staff's recommendation with respect to the improvements in financial statistics, including reporting to the Fund, as presented in Attachment III of the staff report, I understand from Mr. Kafka's statement that these issues are contested by the authorities. I hope that the forthcoming technical mission by the Bureau of Statistics will lead to an early resolution of this problem.

I endorse the staff appraisal, including the recommendation to approve the authorities' request for the delivery of copies of the staff reports to Colombia's bank creditors. In this regard I reiterate, however, that Article IV consultation reports should in general be made available to third parties only on a very restrictive basis, so as to preserve the quality, as well as the openness and frankness, of the consultation procedures.

Mrs. Ploix made the following statement:

I commend the authorities for the continued good performance of the Colombian economy. In the face of a sharp deterioration in the terms of trade, the necessary countervailing actions were taken to maintain the major economic indicators broadly in balance. Another positive feature is the steady level of economic activity, which seems to indicate a somewhat lessened sensitivity of the economy to external conditions.

I broadly share the staff's views on Colombia, yet I would like to stress some elements which should be kept under closer review.

On the fiscal side, although the deterioration experienced this year in the overall position of the public sector remained within manageable limits, the offsetting revenue came mainly from the oil sector and state-owned industries at large. This underscores the rather low level of tax proceeds in total revenue. One way of enhancing the tax base would be to rely more on tariffs and less on quotas in the trade sector. Such a consideration can only strengthen the case for a more rapid dismantling of quantitative restrictions. In the area of public expenditure, it is to be hoped that the shift from energy sector projects to social project financing will be undertaken with the continued involvement of the World Bank.

With regard to monetary policy, the various steps taken by the authorities to cushion the expansionary impact on liquidity of a widening fiscal deficit yielded satisfactory results. Nevertheless, as noted by the staff, credit to the private sector is likely to be slightly constrained this year. At this stage, the risk of a crowding-out effect has not yet materialized, but the authorities might anticipate some remedial action in case it does occur. Specifically, equity financing, and more broadly, the development of the financial market, would help accommodate these financing needs, while at the same time fostering household savings. Enhancement of the private sector savings rate, which is at present fairly low, would also go a long way in keeping the growth of domestic demand under control.

The issue of demand pressure is referred to in the staff paper in connection with inflation. A steady growth rate maintained over the medium term could actually intensify the inflationary risks that are already entrenched in the economy through the wage indexation mechanism. The authorities should therefore be prepared to take all necessary measures to prevent any acceleration in inflation.

Regarding the external sector, the overall picture appears satisfactory, as the economy proved resilient in the face of the rapid decline in coffee exports. The medium-term outlook is also rather reassuring, to the extent that an orderly management of foreign debt seems feasible under fairly reasonable assumptions. Nevertheless, the degree of diversification of exports looks somewhat weak, if one considers that the nontraditional component would account for 37 percent, instead of 30 percent, of total receipts in 1992. As the price-sensitive portion of exports--namely, coffee and oil products--is likely to remain substantial, a more cautious approach would be for the authorities not to preclude any increase in the absolute level of reserves over this period. Given the debt service profile over the next three years, the level of reserves should be kept broadly stable, in relative terms.

I have no objection to the Colombian authorities' request to release the staff reports to their bank creditors, but I would like to emphasize that this should not induce the staff and management of the Fund to compromise the frank nature of the appraisals of the country's economic situation.

Mr. Hodgson made the following statement:

We are in general agreement with the staff appraisal. The Colombian authorities have done an impressive job in adjusting the economy to changing external developments. The comprehensive economic adjustment program implemented in 1985 has shown significant positive results in terms of the fiscal balance, the level of national savings, and the overall balance of payments position. While to some extent sharp increases in coffee prices contributed to the strong performance last year, sound macroeconomic policies are no less important in explaining the recent improvement in performance.

It is particularly noteworthy that the real effective devaluation of the peso since 1982 has led to fundamental changes in the structure of Colombian exports. As the share of coffee in total exports has declined, Colombia has become less exposed to international coffee price fluctuations, and therefore more able to maintain a steady growth path for exports.

There are two areas where we feel the authorities could be more ambitious in their policy design. The first of these is with respect to inflation, which remains in excess of 20 percent. While this rate is relatively low compared with that in other Latin American economies, it can have an adverse impact on confidence, investment, and therefore the prospect for sustained growth. Inflation in Colombia appears to result in part from the general indexation of wages to past inflation, and also from supply bottlenecks in the agricultural and manufacturing sectors. Certainly, maintenance of cautious fiscal and monetary policies is vital if inflation is to be reduced. However, we feel that the authorities should re-examine wage policies to make wage increases more closely related to future inflation, not past, and to productivity growth. Moreover, there is room for further improvements in the foreign exchange system, which, despite some recent liberalization efforts, remains characterized by extensive import licensing, multiple currency practices, and bilateral agreements. The recent liberalization of foreign investment regulations is welcome, but needs to be supplemented by further measures, particularly the replacement of import licenses with tariffs. The present favorable external position gives Colombia an excellent opportunity to accelerate the liberalization process, an opportunity not to be missed.

My second concern is the continuing heavy burden of foreign debt. Colombia has managed to avoid a rescheduling of its external debt, and has been able to secure new commercial bank financing, in part with assistance from the Fund in the form of a special monitoring arrangement. However, debt service ratios will remain high for some years to come, and Colombia has also encountered some delays in securing new private bank financing. These factors suggest that the authorities must continue a very cautious policy toward foreign borrowing, with careful use of the exchange rate to preserve external competitiveness and with little room for departure from the present tight fiscal and monetary policies.

In the present circumstances, we can agree to the authorities' request to provide copies of the staff report to creditors, but I also urge the authorities to maintain and, where possible, strengthen the existing policy stance, which is the best means for Colombia to fully re-establish normal relations with its creditors.

Mr. Lim made the following statement:

We are happy to note that in spite of the large decline in world coffee prices, Colombia has managed to sustain its growth momentum in 1987, as the economy begins to reap the benefits of the authorities' adjustment program toward export diversification. This sustained growth, we think, has allowed the authorities to maintain their prudent macroeconomic policy stance and to resist pressures for economic stimulation, which can only lead to higher inflation.

The staff assessment gives reason for optimism regarding future developments in Colombia, barring wide fluctuations in coffee, coal, and petroleum prices and in international interest rates. Therefore, I will limit my comments to the efficiency aspects of the policy instruments presently being utilized by the authorities.

I agree that the authorities should maintain their prudent fiscal and monetary policy stance, especially as the rate of inflation is still higher than desirable, and flexibility is limited by the country's relatively high external indebtedness. But perhaps the authorities' approach can be improved somewhat through the use of more efficient policy instruments.

In the area of monetary policy, for instance, perhaps the staff can enlighten us on the success of the authorities' open market operations. There may be scope for improving this instrument, and for relying less on the remaining controls on interest rates and the use of high reserve requirements for liquidity management. In my view, the authorities' objective of promoting efficiency and competition in the financial system can best be achieved if the cost of financial intermediation can be reduced by way of low or minimum reserve requirements, and if the authorities can continue to link the remaining regulated interest rates to market-determined rates, with a view to eventually deregulating all interest rates.

In the fiscal area, I have no doubt that the authorities can maintain their expenditure controls, as they demonstrated last year when higher coffee revenues provided the temptation to expand. I can also appreciate the merit of stimulating private savings and investment through the phasing-out of the taxation of the inflation component of financial income. In this regard, I wish to commend the authorities for their success in raising gross national savings significantly in 1986.

On the external policy, I can only reiterate the position of the staff that it is most desirable to accelerate the reduction of the complex restrictions in the exchange and trade system.

I am as optimistic as the staff concerning Colombia's prospects, and I support the proposed decisions.

Mr. Posthumus made the following statement:

The performance of the Colombian economy is indeed commendable; the Colombian authorities have managed the economy quite well. One wonders whether public and political acceptance of timely measures is perhaps greater, once the habit of a policy directed at macroeconomic stabilization has established itself. In any case, I support the staff appraisal, and would like only to emphasize a few points.

While I agree with Mr. Kafka that the importance of a favorable external economic environment for Colombia cannot be overemphasized, it is also true that the economy remains vulnerable, and that continuous efforts have to be made to strengthen it, and seek for it to derive more profit from international trade.

First, the staff mentions that while the authorities recognize the benefits of lower inflation, they are not too optimistic about the possibility of lowering it in the near future. Efforts to modify the system of wage indexation may be necessary, but I doubt that linking pay adjustments to policy objectives for future inflation as well as to past inflation would be helpful. If the expected lower inflation fails to materialize, large pay adjustments might have costly destabilizing effects. Gains in labor productivity through stronger growth in private investment, among other methods, are a slower but a better way to gradually undermine wage indexation as a system.

Second, notwithstanding the positive medium-term outlook for the balance of payments, Colombia's external position is still very sensitive to external shocks, namely, to prices for commodities like coffee and oil, which amount to about 60 percent of exports, and to interest rates. I believe that it is indeed a perfect time for the authorities to eliminate the complex multiple currency practices, extensive import licensing, and other exchange and trade restrictions. Although the reluctance of the authorities to move quickly in this area is understandable, the revision of such policies, if carried out with care, does not necessarily lead to a weakening of the external sector. In particular, by continuing the diversification of Colombia's exports the external sector would be strengthened, and an increasing share of exports in GDP will also mean that the debt service burden will become more manageable. In fact, however, the medium-term outlook shows a decreasing share of exports in GDP.

Finally, I see no reason to object to the authorities' request to transmit the staff report to Colombia's creditors, with the same provisos and understandings as mentioned by Mr. Goos and Mrs. Ploix. However, I think that such arrangements should be submitted to the Board, or at least to management, before the agreement with the banks is made.

Mr. Rieffel made the following statement:

I commend the Colombian authorities for the consistent pursuit of prudent financial policies in the last few years. The benefits of these efforts can clearly be seen in the achievement of a rather high rate of real economic growth, a substantial strengthening of the balance of payments position and, at least by Latin American standards, a fairly moderate rate of inflation.

Such a performance has allowed Colombia to escape the most severe aspects of the international debt problem and, if continued, should result in a full regularization of Colombia's relations with private creditors. The successful conclusion of the special monitoring arrangement with the Fund, and the transmittal of the 1987 and 1988 Article IV consultation reports to the commercial banks as the basis for the new financial arrangements between Colombia and the banks, attest to the progress being made. In that connection, we can support release of these documents. However, I would express a degree of disappointment that, at the end of 1987, it has not been possible to include in this year's report more quantified estimates for 1988.

The Colombian example demonstrates one of the best approaches to achieving an adequate rate of real economic growth, while moving toward a more sustainable external position without extraordinary levels of external financing. Underlying the 5 percent real growth rate in 1986 was a strong growth rate of private fixed capital formation of 15 percent. It would be interesting to know if this pattern continued in 1987, when a similar GDP growth rate is expected, and what private sector investment rate is expected to accompany the 1988 forecast GDP growth rate of another 5 percent. An examination of savings and investment rates through 1986 shows some decline in the rate of fixed capital formation in recent years, mainly in the public sector, while there has been major improvement in public savings, especially by the public enterprises. I wonder how the staff now evaluates the adequacy of the domestic savings and investment outlook.

Strengthening of the fiscal accounts, more generally, can also be seen in the decline in the ratio of the public sector deficit relative to GDP by 5 percentage points between 1983 and 1987. Most of this reflects improvements on the revenue side, especially in the form of a more favorable financial position of the public enterprises and a rise in tax revenue. But the spending ratio has also declined.

Better revenue performance seems to reflect both the effects of tax reform, especially the tax amnesty, and revenue from rising imports, which has been made possible by good export performance. It is encouraging to see that the tax reform of 1986 has resulted in some scaling-down of marginal tax rates, and actions to create a more favorable tax environment for equity financing. The improved profit picture for businesses, and their greater reliance for financing on equity and retained earnings, should be a good omen for future investment prospects. The authorities are to be congratulated on progress made to date in the tax reform field. We also hope that the current study of the problem of revenue earmarking comes to a prompt and satisfactory conclusion.

Financial market reforms do not seem to have progressed nearly as far as reforms in the fiscal area. We are encouraged that the financial position of the banks has strengthened, as indicated by higher profits and a lower share of nonperforming assets in their portfolios. Also, the linking of interest rates charged by several of the Banco de la República's financial funds to market rates is a step forward. Nonetheless, the financial system is still subject to controls on interest rates and to credit allocation mechanisms which raise questions about possible distortions in financial flows. In that connection, we are encouraged that the regulation of foreign direct investment in the banking and other sectors has been somewhat liberalized.

Turning to the external accounts, we are impressed with the strengthening which has occurred in the balance of payments, the accumulation of reserves equal to about 11 months of imports, and the prospect of a fairly favorable medium-term balance of payments and debt outlook. The very sharp real effective depreciation of the exchange rate, in excess of 40 percent since the end of 1984, is evidently having the desired effect on nontraditional exports, adding to the one-time coffee export rise and assisting the coming on stream of energy exports.

Continued exchange rate flexibility will be needed, especially if Colombia continues to experience inflation rates of 20 percent or more. However, we share the views of the staff that the time may be ripe for a more active effort to bring down the rate of inflation. There is a danger that the long record of such high, but rather stable, inflation rates will lead to complacency. Yet, the ease with which inflationary pressures can accelerate has been amply demonstrated in other countries. We would urge the authorities carefully to examine what might be done with regard to wage indexation, the rate of credit expansion, import liberalization, and other policies, in order to bring down inflation.

Some encouraging progress has been made toward liberalization of import licensing, partly with the help of the World Bank. The staff report also indicates that the authorities plan to follow up on the 1985 reform of customs tariffs, although the scope and pace of this action is not spelled out. However, the continuation of a complex and partially discriminatory array of exchange restrictions, bilateral agreements, and multiple currency practices does not seem in keeping with Colombia's improving external position, or with its obligations under the Articles. We join other Directors in hoping that substantial progress can be made in this area in the coming year.

Colombia is continuing to pursue prudent financial policies. It has made good progress in fiscal reforms, and somewhat more limited progress in the area of trade and payments liberalization and financial market reforms. This strategy is already contributing to rather good performance on growth and the balance of payments, in particular. The medium-term prospects for sustaining growth, preserving balance of payments gains and reducing the debt burden appear to be quite good. But there is still room for improvement in bringing down inflation and in extending the structural reform effort. We are confident that the authorities will not fail to take advantage of present opportunities to move in that direction. We support the proposed decisions.

Mr. Tamami made the following statement:

In spite of the sharp fall in the international price of coffee, Colombia's main export item, the authorities' determination to continue the policy stance adopted since 1985 in the context of the 1987 economic program resulted in a satisfactory economic and financial performance in 1987. The significant progress made during 1985 and 1986 in redressing the deterioration of the early 1980s, and in diversifying exports, helped the authorities to react quickly to the decline in coffee prices, thus limiting the adverse impact on the public as well as the external sectors. Real GDP is projected to grow at a rate of about 5 percent in 1987, the overall external position is projected to be in balance, and the public sector deficit is expected to decline more than the program target. The rate of inflation, however, is predicted to rise by about 2 percentage points more than envisaged under the program.

The authorities are to be commended for their efforts in pursuing cautious fiscal and monetary policies, and for maintaining the real effective exchange rate at an appropriate level following the substantial devaluation during the adjustment programs. These policies helped the authorities to enhance the economy's competitiveness and to lay the basis for further diversification of exports, in order to reduce the economy's vulnerability to external shocks.

Given the uncertainties about the world prices of coffee, petroleum and coal, and international interest rates, I agree with the staff that "it is clear that exchange rate policy will need to be kept under close review." However, I am not convinced of the merits of the staff's suggestion that the satisfactory external position of Colombia provides "a good opportunity to accelerate the opening of the economy." Taking into account the staff's argument about the need to keep the exchange rate under close review, and the great sensitivity of Colombia's economy to external shocks, I question whether an acceleration of the process of opening the economy under the present circumstances would serve to maintain a manageable external position.

The authorities' efforts to gradually reduce restrictions on exchange and trade have so far been feasible and commendable steps in the right direction. Measures implemented in the fiscal, monetary and exchange rate areas, particularly those that addressed the difficulties of certain financial institutions, have improved Colombia's medium-term outlook, as outlined in Mr. Kafka's informative statement. The projected overall balance of payments surplus in 1988, and its projected equilibrium in the coming years, demonstrate the appropriateness of the authorities' policy stance.

In concluding, I note the relative improvement in normal relations between Colombia and its bank creditors, which will hopefully lessen the need for Fund involvement in Colombia.

Ms. Kyhlberg said that she agreed with the staff appraisal and with the proposed decisions. As her chair had advocated before, the fiscal and monetary measures implemented by Colombia could usefully be accompanied by further liberalization of exchange and trade restrictions, especially as recent favorable economic developments had strengthened the economy and would facilitate such structural adjustments. Although she was in favor of the decision approving the transmittal of the staff reports for 1987 and 1988 to Colombia's bank creditors, as this was evidence of the normalization of relations between the parties, she wished to support the remarks of Mrs. Ploix and Mr. Goos in wishing that the transmittal would not have the effect of endangering the frank character of the consultation reports.

Mr. Kyriazidis endorsed Mr. Kafka's assessment that Colombia had done exceptionally well in a difficult year. However, as many other Directors had noted, he was perplexed by the persistently high rate of inflation, and particularly by its apparent stickiness. The causes of inflation were unclear and the staff papers did not shed much light on the matter. The budget deficit had been reduced considerably and was now relatively low, so that it could not be considered as a major factor driving inflation; likewise, monetary policy had been prudent, the credit aggregates had grown only slightly above the inflation rate, and interest rates in both nominal and real terms were quite high. Although possible explanations of the driving forces behind inflation included wage indexation and the accelerated depreciation of the exchange rate in 1985, to which Mr. Feldman had drawn attention, ultimately such explanations seemed inadequate, and he would appreciate the staff's comments. Furthermore, it was perplexing that the authorities appeared to have resigned themselves to high inflation, and that despite the obvious seriousness of the problem the staff's assessment of it appeared rather weak. The staff had merely said in the staff report that inflation still needed to be reduced and that success would need to come largely from appropriate fiscal and monetary policies; it was his impression that the staff was evidently prescribing mainly demand-management measures. However, it was generally agreed that appropriate fiscal and monetary policies had been pursued fairly consistently, but little progress had been made in reducing inflation. In fact, an acceleration of inflation was expected for 1987. Consequently, emphasis on demand-management policies did not seem to be the answer.

The staff's contention that modification of the wage indexation system and a more rapid pace of exchange and trade liberalization would help to contain inflation by cushioning the possible adverse effects on output of measures to slow the growth of demand was puzzling, Mr. Kyriazidis observed, and he would appreciate clarification of the point.

The staff representative from the Western Hemisphere Department informed the Executive Directors that the financing package from commercial banks had been concluded, although for an amount that was slightly less than that requested by the Colombian authorities. The amount requested was US$1,060 million, and the amount that had been committed finally was US$1 billion. The authorities intended to go to the market with bonds or floating rate notes for the difference. The new loan would probably be signed by December 30, but there might be some delays. Disbursement of the loan was to be made entirely in 1988. Conclusion of the loan agreement had taken more time than either the banks or the authorities had anticipated, and could not be attributed to any single factor.

Several Executive Directors had commented on the paucity of information about 1988 in the staff report, the staff representative recalled. Although comprehensive provisional information concerning the fiscal, monetary, and balance of payments outlooks for 1988 had been made available to the staff at the time of the discussion in August 1987, which was highly unusual given the date of the mission, the fact that the budget had not yet been submitted to Congress caused the authorities to be uncomfortable about divulging a greater quantity of detailed statistics about 1988. Furthermore, as the discussions with the Fund were in the character of a consultation rather than a negotiation for a program, the authorities believed that the presentation of their policies and objectives, as had been done in the staff report, was sufficient.

With respect to exchange rate policy, the staff representative went on, the authorities intended to maintain their external competitiveness; there had been a very large real currency depreciation in the last two or three years. However, the nominal rate of depreciation had decelerated in 1987 compared to that in 1985 and 1986, and although the authorities intended to adjust the rate in nominal terms so as to maintain the level of external competitiveness, they did not anticipate making gains in real terms. Thus, exchange rate policy should not contribute to inflationary pressures.

Many Directors had spoken about the relationship between indexation and the exchange rate and inflation, the staff representative noted. Although inflation in Colombia was persistently sticky, at least it was stable, even though at a level that was a cause for concern. The authorities had agreed that the system of wage indexation had been a factor in the stickiness of the inflation rate. Increases in wages were determined by the level of inflation of the previous year, which contributed to a rate of inflation that, although possibly no higher than that of the previous year, would probably also not be any lower. Consequently, as some Executive Directors had suggested, a more forward-looking, rather than backward-looking, wage indexation system might contribute to a reduction of inflationary pressures. There was, of course, the danger, of which the authorities were fully aware, that if such a change were implemented and inflation did not in fact subside, the exact opposite would happen, as there would be pressure to adjust wages even more frequently, thus exacerbating inflation. But a positive signal was that the Minister of Finance was proposing public sector wage adjustments which would be somewhat below the current rate of inflation.

With regard to the impact of the exchange rate on inflation, the large real depreciation in the period 1985-86 might have played a role in the slight acceleration of inflation over the period 1985-87 compared to the period 1983-85, the staff representative added. However, in the view of the Colombian authorities, an even more important factor in inflation which had not been raised in the staff paper was the swings in food prices. This was a function, first, of crop production and the weather, and second, of food imports from neighboring countries, closely related to exchange rate policies in those countries. The impact of these swings could be observed in the decline in the rate of inflation in 1983-84, when relative exchange rates had favored imports from neighboring countries, particularly of food items, which had reduced the pressure on domestic food prices. This situation had now been reversed. In 1987, prices would have risen by only 20 percent--compared with an actual increase of 23 or 23 1/2 percent--if food prices had been excluded, which showed the impact of food prices on the inflation rate. A 20 percent rate of inflation was about the same rate as that of the previous year. Even so, the underlying rate of inflation remained a matter of concern, and the authorities were attempting to pursue monetary, fiscal, and wage indexation policies which would contribute to its gradual reduction.

One Director had remarked that although progress in diversifying the Colombian economy had been made it had not been particularly remarkable, the staff representative continued. However, it might be observed that if the level of new exports such as coal and oil were excluded, the increase in the level of other nontraditional exports was more impressive, and was evidence of the continuing diversification of the economy.

The Banco de la República had been active in conducting open market operations in order to keep the overall expansion of credit in line with the macroeconomic objectives, and had been very successful, the staff representative observed. Domestic liquidity equivalent to approximately

1.5 percent of GDP had been absorbed through the Banco de la República's open market operations in 1987. These operations were not costless for the Banco de la República, of course, but the authorities felt them to be the best way of absorbing excess liquidity. Although the reserve requirement mechanism could be activated to serve the same purpose, the level of reserve requirements was already high, and any increase might have affected the profitability of banks. There might also have been an impact on the spread between passive and active rates.

With respect to the trade system, the staff representative from the Western Hemisphere Department concluded, significant reforms to customs duties had been introduced in 1985-86, in the context of an export diversification loan from the World Bank. Nominal tariff rates had been reduced from 61 percent in 1984 to about 50-51 percent in 1986, the standard deviation had been reduced from 29 percent to 16 percent, and the average rate of effective protection had fallen from 61 percent to around 54 percent. Although progress had been made, there was still room for a further reduction of protection. The authorities had indicated to the staff that additional reforms would be implemented, especially because recent economic developments made it propitious to embark in a gradual way on internal and external structural adjustments, encompassing reforms and liberalization of the trade system, so as to facilitate sustained growth over the medium term.

Mr. Kafka thanked Executive Directors for their comments and their interest in Colombia, and for the authorization for Colombia to transmit the 1987 and 1988 Article IV consultation reports to its creditor banks under the appropriate safeguards. He acknowledged the staff's responses, and noted that as Colombia had had some unfortunate experiences with the rapid removal of restrictions, the authorities' inclination to move slowly in that area appeared justified and would need to be borne in mind.

Recalling that many Directors had mentioned the rapid pace at which Colombia was normalizing relations with its creditors, Mr. Kafka commented that notwithstanding the ultimately successful efforts of the authorities and of the Fund toward that end, it had been a complicated and protracted task, and evidence that even when countries moved forward rapidly and followed all the correct policies, the re-establishment of normal relations could be difficult.

With respect to the many observations made about inflation in Colombia, Mr. Kafka mentioned that the inertial element in inflation could not be ignored. When inertia was present, the only ways of eliminating inflation rapidly were either to cause a monetary shock of the type which Argentina, Brazil, Bolivia, and Israel had attempted, a difficult undertaking, or to promote a major recession, which was not to be recommended, certainly not in Colombia where unemployment was already quite high. If the rapid routes to eliminating inflation were not appropriate, the only course was its gradual elimination, the monitoring of inflation to see that it did not accelerate while using favorable supply shocks, productivity increases, and other such positive developments to chip away at inflation, which was the Colombian authorities' philosophy. In conclusion, he assured the Board of Colombia's intention to continue its prudent policies.

The Acting Chairman made the following summing up:

Directors commended the authorities for the continued application of prudent economic policies that had contributed to the favorable economic performance in recent years. Strong economic growth, an improved rate of national savings, and a satisfactory external position were maintained in 1987, in spite of the sharp drop in the export price of coffee.

Directors welcomed the authorities' intention to maintain in 1988 a policy stance broadly similar to that of 1987. Nonetheless, most speakers believed that the authorities should place more emphasis on reducing inflation as a means of improving the conditions for economic growth in the medium term. While recognizing that there did not appear to be an immediately recognizable dominant cause of inflation, Directors encouraged the authorities to consider several approaches, not limited only to continued prudent fiscal and monetary policies, but including, for example, modifications in the system of wage indexation and an acceleration in the reduction of exchange and trade restrictions.

Directors noted the tax reform, which was designed to raise personal savings and equity investment. They observed that the authorities' intention was to keep the thrust of fiscal policy in 1988 about the same as in 1987, but commented that achievement of this objective required the tight control by the authorities of increases in outlays, and the exercise of caution about the intended shift in the composition of investment outlays toward social investment.

Directors were of the view that while enough room seemed to have been allowed for growth of credit to the private sector, developments in this area would need to be monitored closely. Directors encouraged the authorities to pursue reforms of the financial system with a view to reducing the cost of intermediation and broadening the financial markets.

Directors believed that the exchange rate policy followed by the authorities had played an important role in helping Colombia to diversify its exports. Directors agreed with the authorities' view that the current level of the real exchange rate was broadly adequate, but most stressed that it was necessary to keep a close watch over cost-price relationships and to be alert to developments in the balance of payments in order to ensure the preservation of the country's external competitiveness.

Noting Colombia's medium-term balance of payments prospects, a number of speakers encouraged the authorities to pursue, with caution, the further liberalization of the exchange and trade system, including foreign direct investment. Continued progress in these areas would raise efficiency and could contribute to the lowering of inflation. Directors remarked that although the debt service burden appeared manageable, particularly in view of the recent strengthening of the external sector, the burden was still high enough, and Colombia's external position was still vulnerable enough, to warrant the continuation of a cautious approach toward foreign borrowing and the level of international reserves.

Directors were encouraged by the success of the authorities' efforts to secure commercial bank financing for 1987-88, which would be used to amortize debt with commercial banks. They hoped that the loan secured through this financing would be a step toward regaining voluntary access to international capital markets.

It is expected that the next Article IV consultation with Colombia will be held on the standard 12-month cycle.

The Executive Board then adopted the following decisions:

Decision Concluding Article XIV Consultation

1. The Fund takes this decision relating to Colombia's exchange measures subject to Article VIII, Sections 2 and 3, and in concluding the 1987 Article XIV consultation with Colombia, in the light of the 1987 Article IV consultation with Colombia conducted under Decision No. 5392-(77/63), adopted April 29, 1977, as amended (Surveillance over Exchange Rate Policies).

2. Colombia's restrictive practices are maintained pursuant to Article XIV, except that it continues to maintain a complex system of restrictions on payments and transfers for current international transactions and multiple currency practices, as described in SM/87/285, that are subject to approval under Article VIII, Sections 2(a) and 3. The Fund welcomes the process of simplification of the exchange system initiated in the recent past and urges the authorities of Colombia to continue this process. The Fund notes that Colombia maintains bilateral payments agreements with two Fund members and encourages Colombia to eliminate them as soon as possible.

Decision No. 8764-(87/179), adopted
December 23, 1987

Release of Information

The Fund approves the request of Colombia to transmit to its creditor banks and other creditor financial institutions party to the US$1,060 million loan to Colombia, the staff reports for the 1987 and 1988 annual Article IV consultations with the Fund, on the understanding that the recipients of the reports will have assured Colombia that the reports will not be used for any purposes other than those of that loan to Colombia, and will be kept confidential, and that the 1988 staff report shall not be transmitted by Colombia earlier than two weeks after its circulation to members of the Executive Board.

Adopted December 23, 1987

3. ETHIOPIA - 1987 ARTICLE IV CONSULTATION

The Executive Directors considered the staff report for the 1987 Article IV consultation with Ethiopia (SM/87/266, 11/17/87, and Cor. 1, 12/22/87). They also had before them a background paper on recent economic developments in Ethiopia (SM/87/288, 12/9/87) and an information notice on the real effective exchange rate of the Ethiopian birr (EBS/87/270, 12/22/87).

Mr. Abdallah made the following statement:

The momentum of economic growth which Ethiopia achieved in 1985/86 was maintained in 1986/87, although at a somewhat decelerating rate, owing to the unfavorable external and domestic environment. Nevertheless, a combination of prudent fiscal and monetary policies, and the continuation of a policy of careful management of available scarce resources for enhanced economic efficiency, resulted in an estimated real GDP growth rate of 8.1 percent, while actual aggregate output growth for the preceding year was 6.7 percent. However, owing, among other things, to huge terms of trade losses, the overall balance of payments, which had been in surplus, turned into a deficit, as both public transfers and net capital inflow declined, with worsening medium-term prospects following the return of a drought--reportedly of great intensity.

Aware of the pervasive adverse impact of droughts and the terms of trade deterioration, the authorities have embarked on a number of measures designed to address the situation within the prevailing socioeconomic system. To expand production, a new investment policy is in place, and the limit of investment capital for the private sector has been doubled to 1 million birr. Furthermore, in recent years the authorities have made moves to attract foreign investment by offering attractive terms. As for pricing policy, the authorities hold the view that the performance of their type of economy is highly dependent on natural conditions, and they do not believe that decisions on optimal allocation of resources should be left completely to the price system. Nevertheless, on the basis of a recent review of prices, some liberalization has been effected. Electricity prices for commercial and industrial use were increased by up to 75 percent in 1986 while producer prices for the main cereals were raised in 1982/83. Within the last year, prices of some manufacturing products, notably beer, textiles, and edible oils have been revised, and a high-level committee formed in 1986 is carrying out a comprehensive study on issues relating to fixed prices.

In the view of the Ethiopian authorities, agriculture remains the main priority, and a number of measures are being implemented to address the existing natural (weather), technological, organizational, management, and manpower problems in order to expand production in the sector. Stress is being laid on the implementation of irrigation projects, a resettlement program in the sparsely inhabited but fertile regions, and on the provision of improved seeds. To facilitate the implementation of the planned peasant agricultural development program, the Government has approved measures as recently as last week, to increase producer prices for major food grains and some export crops.

Traditionally, Ethiopia's fiscal management has reflected a cautious policy stance, which the authorities maintained in 1986/87. Further reduction in the fiscal deficit remains a major objective which has guided revenue and expenditure considerations at various levels of administration. As a matter of policy, implementation of even desirable projects was quite often adjusted to take account of the availability of financial and other resources.

Marked improvement in revenue performance was recorded in the 1986/87 fiscal year owing, partly, to a number of new measures introduced to generate more revenues and, partly, to improvement in revenue collection procedures. Excise duties were imposed on some brands of beer, while excise tax rates on some locally produced cigarettes and customs duty on imported tobacco products were increased. This, together with improved customs administration, resulted in a 7.3 percent rise in government revenue in 1986/87, more than in the preceding year. The achievement of such a favorable revenue position, despite the expiration of the drought relief levy and the reversal of favorable international factors such as the movements in coffee and oil prices, underscores the great success of the authorities' revenue performance. A prudent pattern of expenditures was maintained, as in previous years. Except for social services and interest payments, government expenditure fell in virtually all other categories in 1986/87 below the budgeted figures and the actual figures for 1985/86. However, the 1987/88 budget provides for a significant increase in expenditure, on the order of 25.2 percent of GDP, much of it directed toward capital projects, in line with the Government's strategy of expanding production and stimulating growth in a manner consistent with investment priorities of the three-year subplan (1986/87-1988/89).

Monetary policy remained tight, directly controlled, and guided by the credit guidelines of July 1986; the outcome was the decline in the rate of expansion of broad money in 1986/87. Credit to the Government, which recorded an increase over the level of the preceding year, was largely earmarked for financing the budget deficit. With the termination of the drought relief levy and less reliance on external sources, greater recourse was made to domestic bank financing of the government deficit. Another factor in the recent credit expansion has been the policy of reviving economic activity through provision of increased credit to the productive sectors, as well as for rural development. This, in part, explains the increased lending by the Commercial Bank of Ethiopia to public enterprises, cooperatives, and the private sectors. Although Ethiopia operates a centrally planned economy with interest rate policy playing a limited role, they have altered the level and structure of interest rates with effect from July 1, 1986. In general, the rates have been lowered, although they remain positive in real terms, and greater differentiation in interest rates has been implemented for the different sectors of the economy in order to stimulate investment, particularly in the preferred sectors.

On exchange rate policy, the authorities note that the staff has urged that work on an internal study on the effects of exchange rate action be accelerated. While cognizant of the views and concerns of the staff, they do not believe that an exchange rate adjustment at this time would bring about an improvement in the balance of payments. The question of devaluation of the Ethiopian birr and the choice of an appropriate peg became an issue when the real effective value of the birr increased from the beginning of 1981 to late 1985, at the time of the appreciation of the dollar. Although the authorities kept the situation under review, they saw no need for action, since reserves were thought to be at relatively comfortable levels and imports were not expected to be generally affected, as most were not denominated in dollars.

The Ethiopian authorities strongly hold the view that the birr has been depreciating with the dollar since late 1985. According to them, the birr has depreciated by 43.4 percent in real effective terms between March 1985 and March 1987, and as the dollar is now much lower than it was in March, the birr is thought to have depreciated further. Therefore, the staff's recommendation of an accelerated timetable for the internal exchange rate study should not be construed to mean that the time is ripe for exchange rate action; the authorities maintain that evidence from prevailing economic conditions points to the contrary. They believe that the depreciating birr and the drought make any exchange rate action at this stage inopportune. Nevertheless, the authorities are aware of the role that the exchange rate can play, and they intend to take appropriate action when the drought situation has been overcome and normal economic conditions restored.

With regard to trade and exchange restrictions, the authorities feel disappointed that the staff has not recommended approval by the Executive Board of Ethiopia's restrictions on payments and transfers for current international transactions. At the time of the consultation, they had reiterated to the staff that the measures in force should not be construed as restrictive, but only as an exercise of prudence in the face of very difficult circumstances. They stressed that given the persistent drought situation, the worsening terms of trade, the instability of coffee prices, the heavy reliance on a single export crop, and the low levels of external aid, a country such as Ethiopia, which is one of the least developed in the world, must, of necessity, resort to such restrictions, in order to conserve the scarce foreign exchange needed to ensure availability of essential supplies. They believe that if the current trade and payments measures were relaxed in the existing circumstances, the reforms implemented so far would be frustrated, and the capacity of the economy to absorb internal and external shock would be severely curtailed.

In urging the Board to approve the retention of these measures, the authorities stress that an earlier approval was granted in the years when weather conditions were not as severe as they are now, and that a denial of approval when it is most needed would complicate their economic management problems, and render it more difficult to muster external support. They strongly urge the Board to note that the measures which the Fund considers restrictive are there out of necessity as a matter of survival, which, among other things, have helped the country to remain current in its external payments obligations and to build up reserves. At end-June 1987, reserves were equivalent to about 15 weeks of imports. The authorities had understood that these achievements had won for them the Fund's recognition and welcome in the past. It is their conviction that the relaxation of the measures should in no way be connected with the question of structural adjustment arrangements, as their need for such arrangements should be viewed within a broader framework and should take full account of the country's social, economic, and political objectives.

Notwithstanding the authorities' strong determination to put the economy on a firm growth path, the persistence of imbalances and the return of severe drought conditions must affect medium-term prospects and render the task of finding an effective and durable solution to Ethiopia's economic and financial problems much more difficult. In appraising Ethiopia's economic performance, there must be a recognition that whatever the policy changes which may be envisaged, not much of durable impact can be achieved in the present circumstances without adequate and timely concessional external financing. The international community is urgently invited, therefore, to show greater understanding and solidarity with the authorities at this critical stage in the national life of Ethiopia.

Mr. Rouai made the following statement:

Since our last Article IV consultation with Ethiopia, the authorities have made significant progress in sustaining a rate of growth of real GDP higher than the rate of population growth, in reducing both the fiscal and current account deficits, and in controlling inflation. The authorities have also continued to devote more effort to improving social services, in particular, education, health, and resettlement, as well as to the villagization programs, so as to improve the standard of living. In this respect, it is worth noting that the literacy rate has increased from 7 percent in 1973 to over 50 percent in 1987, and primary school enrollment has doubled to over 40 percent of the school-age population in the same period. The authorities are also to be commended for remaining current in their servicing of external financial obligations despite the severe economic and financial problems they continue to face.

Our review of the Ethiopian economy should keep in mind the country's exceptional circumstances. Per capita income, of only SDR 96, is the lowest in the world; severe droughts continue to dramatically affect the population, creating significant food shortages and famine and causing widespread disease and loss of life. In normal circumstances, measures to reduce internal and external imbalances and to improve the country's overall performance, would be called for. However, in light of Ethiopia's unusual prevailing circumstances we believe that the most urgent task is to do whatever is humanly possible to feed the population and to provide essential medical care.

The present drought is as severe as that which occurred in 1984-85, and the humanitarian organizations have projected that almost 1.3 million tons of food will be required as emergency assistance for 5.2 million people in Eritrea, Tigray, and other affected provinces. Only 236,000 tons have been committed so far, clearly far below the minimum requirement. Therefore, Ethiopia remains badly in need of further international humanitarian assistance, and the international community should be urged to provide generous aid so as to enable the country to import the necessary food, equipment, and medical supplies, and to improve local transportation and distribution. The flow of aid also should not be interrupted, so as to avoid the re-emergence of huge camps of famine victims as during the 1984-85 drought, where as many people were killed by disease as by starvation. I would like to ask the staff about the possibility of providing Ethiopia with the kind of emergency assistance that has been provided to some other members in the past. I am confident that the Fund's support in this respect would not only help Ethiopia, but would also serve to improve the image and the cooperative character of this international institution.

I am heartened by Mr. Abdallah's statement that agriculture remains the Government's main priority. I further welcome the resettlement and villagization programs being conducted in the country's less inhabited, but potentially productive, regions. The results, including the resettlement of 158,000 heads of family, the construction of 183,000 dwelling units, and the villagization of over 8 million people, are encouraging and should be pursued, so as to improve efficiency in providing essential services to the population. Increased emphasis on the cultivation of selected products in otherwise marginal areas and the use of improved seeds, combined with the implementation of labor-intensive irrigation projects, should help the authorities to alleviate food shortages and to achieve self-sufficiency in certain products. The support of the World Bank remains vital to improving agricultural production, through increased incentives, adequate infrastructural support, and greater efficiency in agricultural marketing and grain distribution.

Regarding exchange rate policy, Ethiopia is suffering not from a lack of competitiveness but rather from a dearth of the resources needed to increase exports. I therefore concur with the authorities on the potential adverse side effects of further depreciation of the birr on the budget, inflation, and income distribution. The internal study to be conducted by the authorities on these effects would be helpful in assessing the need for further exchange rate action.

On the external side, the country remains vulnerable to adverse developments affecting coffee exports, and to the decline of imports resulting from the curtailment of grain and commodity aid. Furthermore, as indicated by the staff, prospects do not appear promising for a substantial reversal of the declining trend in external aid commitment and disbursements to Ethiopia. This is very disquieting and is an area of great concern for the authorities.

While the authorities have used the meager available external resources to remain current in their external financial obligations, I note with great concern that new external commitments took the form of suppliers' credits, resulting in a further deterioration in the already high debt service ratio. I therefore repeat my plea to the international community to increase its humanitarian aid and concessional financial support to Ethiopia, which receives the lowest amount of external aid per capita in sub-Saharan Africa.

Finally, I support Mr. Abdallah's position regarding the approval by the Executive Board of Ethiopia's restrictions on payments and transfers for current international transactions, on a temporary basis. Given the exceptional circumstances of Ethiopia, I concur with the authorities that the existing restrictions are required for managing the scarce foreign exchange resources, so as to ensure the availability of essential supplies, and to help the country remain current in its financial obligations.

Mr. Santos made the following statement:

It is encouraging to note from the staff report that the broad-based improvement in Ethiopia's economy that was evidenced in 1985/86 strengthened in 1986/87. Real GDP continued to grow at a brisk pace, while domestic prices fell. The fiscal deficit was reduced, with revenue increasing at a faster rate than expenditure. This encouraging picture was blurred, however, by the fall in the world price of coffee.

While progress has been achieved in many areas, much still needs to be done to lay the foundation for durable economic growth. This task will be more difficult in the face of another devastating drought that is prevailing in the country. Since the country suffers from such extreme variations in the weather, concentrated efforts will be needed to find ways to improve agricultural yield and diversify the productive base of the economy.

In order to improve agricultural yield, measures are needed both on the technical and the financial side. In the technical area steps have been taken to expand production, as described in the staff report; but additional measures could be taken with regard to pricing policies in order to provide farmers with the necessary incentives to increase output. The various studies being undertaken indicate that the authorities are conscious that a problem may exist with current pricing policies. Therefore, I would urge them to review these policies in light of these studies, and to take full account of production costs in determining producer prices. In this context, I note from Mr. Abdallah's statement the recent increase in producer prices for some foodgrains and export crops.

With respect to the diversification of the economy, the mining sector seems to hold a large potential for development, which will thus make the economy more resilient to climatic changes. In that context, I welcome the measures being taken by the authorities to encourage the participation of private domestic as well as foreign investors in the development of that sector. However, in view of the size of the investment needed, the investment policy must be kept under review and incentives increased, if necessary, to attract private investors. At a time when concessional loan commitments have declined significantly and the terms at which Ethiopia may borrow have deteriorated, foreign investment can be an important source of external financing.

On exchange rate policy, it should be mentioned that despite the sharp depreciation in the real effective exchange rate of the birr and a 24 percent reduction in the volume of imports, the adverse effects of the decline in the price of coffee could not be reversed, and the external current account deficit worsened. This is an example of how external factors can defeat the best efforts of national authorities to improve the economic prospects of their country. In the case of Ethiopia, this is even more unfortunate, as the authorities are taking courageous steps to develop the economy, despite the odds against them. This type of adverse development might also explain the reluctance of the authorities to follow the staff's suggestions regarding the exchange rate. Furthermore, the birr has depreciated sharply as a result of the depreciation of the U.S. dollar, and any further action in the area of the exchange rate would probably have more costs than benefits. I share the authorities' view that there is a need to be careful before making any move with regard to the exchange rate in the present circumstances.

With regard to trade and exchange restrictions, I am disappointed that the staff has not recommended, as in the past, approval of the present policy, especially in the face of the country's very difficult circumstances. In the special case of Ethiopia, a relaxation of current trade and payments measures could have serious adverse effects on the economy. Moreover, these restrictions have helped Ethiopia to increase its foreign exchange reserves to the equivalent of 15 weeks of imports. Nevertheless, I would urge the authorities to keep their exchange and trade policies under constant review.

Finally, I support Mr. Abdallah's call to the international community for greater financial aid for Ethiopia. This financial assistance should not be drought related only, but should be aimed also at developing Ethiopia's many natural resources. I ask Mr. Abdallah to convey the best wishes of this chair to his authorities.

Mr. Enoch made the following statement:

After only a partial recovery from the 1984/85 drought, Ethiopia faces a renewed drought of similar severity. We express our deepest sympathy for the country. Nevertheless, we endorse the staff report's conclusion that major policy adjustments are needed in a number of areas. I will cover only a few of these.

First, I emphasize that we see proper adjustment of agricultural producer prices as a central element of the recovery program for Ethiopia. Consequently, it is disappointing that the authorities apparently do not see the connection between raising these prices, which have been virtually unchanged since 1979, and increasing production. It is, however, encouraging that agricultural pricing has been reviewed, and I join with Mr. Santos in hoping that the authorities can take account of the results of the review, and agree to increase prices at an early date.

Second, the projected fiscal deficit for 1987/88, at 14.3 percent of GDP, represents a significant departure from the fiscal discipline of the 1970s and early 1980s, when the deficit was kept consistently below 5 percent of GDP. Although I recognize that much of the fiscal deficit is accounted for by projected capital expenditures that are unlikely to be realized, so that the actual deficit may be less, the deficit outcome still seems likely to require excessive borrowing. It seems unfortunate that the authorities have not been able to identify savings elsewhere to offset the proposed increase in the capital investment program. Maintaining expenditures constant in nominal terms is an impressive achievement when prices are rising, as the staff paper notes; when prices are falling, as in Ethiopia, one might perhaps hope to achieve more.

Third, I am concerned that the authorities do not appear to see that action is required on the exchange rate, despite the divergence of between 70 and 100 percent in the rate between the official and the parallel markets. I regret that the authorities have refused, at the present stage, the offer of a joint study of the exchange rate with the Fund. On the basis of the staff paper, the balance of payments projection in Scenario B appears unlikely. Unchanged policies, as assumed in Scenario A, are expected to generate financing gaps equivalent to 2 percent of GDP each year from 1989, and even this projection relies on what seems to be a highly optimistic assumption of export growth of 33 percent to 1991. Given the questionableness of this outlook, I would have considerable doubts as to whether the projection of a declining debt service ratio, as indicated in Table 6, is in fact realistic.

One might also question the proposed strategy of continuing to compress the salary ranges of the civil service. Elsewhere in Africa, the opposite policy has been the central plank of civil service reform, and I question whether the motivation and quality of the civil service can be maintained as differentials continue to be eroded.

Finally, last year there were some indications that Ethiopia might be interested in a structural adjustment arrangement, and I would be interested to know from the staff whether negotiations for it have now been abandoned.

Mr. Rieffel made the following statement:

In our last discussion of Ethiopia almost 18 months ago (EBM/86/174, 7/30/86), the prospects for the Ethiopian economy had brightened after a very difficult period of drought. Unfortunately, the prospects at the present stage are not quite so bright, for two reasons. First, there has been a further recurrence of drought. Second, the policy stance of the Ethiopian authorities does not appear to be growth oriented.

As one of a handful of Fund members with centrally planned economies, Ethiopia has certain advantages over other Fund members in managing scarce foreign exchange resources. As a consequence, Ethiopia has been able to avoid arrears during a period of balance of payments strains, and is to be commended for increasing its foreign exchange reserves as well as for meeting all of its financial obligations to the Fund.

Similarly, as a centrally planned economy, it is relatively easy for Ethiopia to control the creation of credit, and as a consequence Ethiopia has not resorted to inflation as a response to internal and external imbalances. Moreover, the authorities have been able to maintain positive real interest rates within the context of an interest rate system that provides for some flexibility.

On balance, however, the disadvantages associated with central planning appear to outweigh the advantages in the particular case of Ethiopia. Generally speaking, structural rigidities in the economy that have been introduced since the 1974 revolution appear to be the main constraint on the economy's growth potential. These rigidities are largely reflected in pricing policies.

To begin with the price for foreign exchange, the staff report notes the fixed relationship between the birr and the U.S. dollar that has been maintained for 14 years, and concludes that the birr is substantially overvalued. We share this assessment. In his statement, Mr. Abdallah has noted the intention of the Ethiopian authorities to take appropriate exchange rate action when normal economic conditions have been restored. We welcome this positive attitude, but urge the authorities to move more rapidly in this area by accelerating action on a joint study with the Fund, rather than undertaking an internal study of the effects of an exchange rate adjustment. We believe that a substantial change in policy, including the adoption of a system with some built-in flexibility, would be needed if Ethiopia were to seek access to IMF resources, either ordinary or concessional.

Incidentally, I was struck by the reference in the staff report to a sharp increase in suppliers' credits in the 1985/86 fiscal year. Does the staff know to what extent these credits are guaranteed by official agencies in the country of the supplier? Furthermore, if these are largely guaranteed export credits, would it not be appropriate for the staff to call attention to this development at an upcoming meeting of the Paris Club?

Turning now to producer prices, we agree with the authorities that higher production does not necessarily result from higher producer prices; my own country is one of the few where higher production has sometimes resulted from lower producer prices. But I have the impression that the authorities place a high priority on raising production, and that they recognize that prices are relevant. For this reason, we are disappointed that the Council of Ministers has not yet acted upon the study of agricultural pricing that was begun in 1986. I would also like to underscore the importance of rationalizing state farms and improving grain marketing for achieving the objective of higher agricultural production.

Industrial pricing is a third area under study where the results seem highly predictable, at least in terms of the need for adjustments and the direction of the adjustments, if not in terms of the magnitude of the adjustment for specific commodities. Again, we urge the authorities to move decisively from study to implementation. In the same area, we welcome the recent initiatives to encourage private entrepreneurship, but share the view of the staff that more can be done to encourage the private sector to contribute to economic growth. In parallel with steps in this direction, the authorities should move vigorously to strengthen the financial position and management of the public enterprises.

Turning briefly to fiscal policies, while I have noted the staff's explanation of why the 1987/88 budget deficit is likely to be smaller than the target of 14.3 percent of GDP, the possibility that the deficit in the current year could be twice last year's level is disturbing. I have also noted the importance of capital expenditures in the projected increase, and would appreciate knowing the views of the World Bank staff on the size and composition of the public investment program.

The medium-term scenarios presented by the staff are helpful in putting in perspective the policy choices the Ethiopian authorities face. The advantages of Scenario B in terms of both economic growth and balance of payments viability are dramatic, and we hope the authorities will turn onto this path.

Finally, I have noted Mr. Abdallah's appeal to have the Board approve Ethiopia's exchange and trade restrictions. The argument that the Board has approved essentially the same restrictions at a time when they were less justified is a powerful one. Nevertheless, I believe that consideration of the authorities' policy stance is more important than consideration of the economic circumstances facing the country in taking a position on whether or not to approve such restrictions. From this perspective, the policy stance of the authorities seems less appropriate now than it did in mid-1986, and therefore we support the staff recommendation that the restrictions not be approved.

Mr. Rebecchini made the following statement:

The Ethiopian authorities are to be commended for the progress they have achieved in spite of severe external conditions. In 1986/87, real GNP is estimated to have grown at a rate of about 8 percent, consumer prices have decreased, and fiscal and monetary policies have been broadly appropriate. In contrast, progress in the structural domain has been less than satisfactory. As we stated at last year's discussion, we regret that the authorities continue to be reluctant to reform the price system and correct the exchange rate. These measures would consolidate the foundation of the development process. The country needs to expand and diversify its productive base and reduce the external constraints in order to achieve a sustained and stable rate of growth. This can best be achieved in a system that provides the necessary incentives and market signals. I will comment on demand policies, pricing policies, and the exchange rate.

Demand policies have been appropriately managed in the past so as to reduce imbalances and set the ground for growth. The cautious stance of monetary and fiscal policy should be continued in the coming year, and we welcome the indications provided by Mr. Abdallah that further reduction in the budget deficit remains a major objective of the administration. Improvements should come from both sides of the budget: on the expenditure side, by maintaining a flexible policy for capital expenditures based on the availability of adequate financing; and on the revenue side, by improving tax administration and collection. Also, there may be scope for cuts in price subsidies, which have increased about threefold in the last year, as indicated in Table 28 of the report on recent economic developments.

On pricing policies, we share the staff's view that prices, particularly agricultural prices, should be adjusted, and that market mechanisms should come to play an increasing role in the economy. Price measures should be integrated into the reform of the agricultural marketing system. The authorities should be encouraged in this respect by the success of other comparable countries in liberalizing the price system in order to create incentives for production and to achieve self-sufficiency in the agricultural sector. While we welcome the few measures adopted recently by the authorities as a step in the right direction, we continue to urge them to act decisively in this area. Actions should be taken along the lines of the recommendations of the interministerial committee study on agricultural pricing, and of the World Bank. The authorities should also continue to pursue initiatives to expand the role of private entrepreneurship and to attract larger amounts of foreign direct investment. We urge them to accelerate this process and provide clear and consistent signals to the private sector, both domestically and abroad.

On exchange rate policy, the maintenance of an appropriate exchange rate level is one of the most powerful factors in stimulating growth, as many speakers noted in our last discussion on growth. We agree with the staff's recommendation of substantial exchange rate action, especially in view of the objective of export expansion and diversification. We wish to emphasize, however, that exchange rate policy should be viewed as an integral part of broader pricing policy. In order to benefit fully from the expenditure-switching effects of exchange rate devaluations, the existence of a flexible and realistic set of domestic prices is crucial. Reform of the pricing system should therefore logically precede the realignment of the exchange rate. This should be interpreted not as an argument for delaying the exchange rate adjustment, but rather for accelerating price reforms.

Finally, on the issue of approval of the restrictions on payments and transfers for current international transactions, while we understand the severe difficulties the country faces, we remain unconvinced by the authorities' arguments for refusing to adopt any measure to reduce the restrictions in place. In view of the very clear indications provided by the Board at the time of the last discussion, and in order to emphasize the importance that the Board attaches to this matter, we support the proposed decision.

Mr. Prader inquired whether the request put forward by several Directors for exceptional international assistance because of the return of severe drought conditions in Ethiopia was supported by the Ethiopian authorities.

Mr. Hogeweg made the following statement:

I would like to focus on only a few issues, which are to my mind crucial for Ethiopia's future development. The Ethiopian authorities undoubtedly follow prudent and cautious policies in a number of areas, for which they should be commended. I note especially fiscal policy, credit policy, and the absence of any external payment arrears in spite of Ethiopia's difficult circumstances.

It is clear that Ethiopia should aim to diversify its crops and strengthen its export base, in order to make the economy less vulnerable over time. Dependence on imports of food, periodically on a huge scale with the onset of droughts, should be diminished as much as possible. Also, in view of the rate of population growth, economic growth is clearly needed. With due respect for the socioeconomic system within which the authorities prefer to operate, I believe the staff has made it clear in the medium-term scenarios that measures to increase incentives to producers, to remove some clear price distortions, and to allow more generally for a freer flow of resources in the economy, would be highly conducive to the authorities' own ultimate economic objectives. Having said this, I realize there are formidable problems to be overcome; especially in the case of Ethiopia it is very difficult to take measures of structural adjustment while trying to cope with emergency situations.

Monetary policy seems to have a primarily allocative role, rather than a macroeconomic character. Credit ceilings are specified by sector, and I understand that the change in the interest rate structure also primarily serves the allocation of credit over sectors. These artificial price signals and implicit subsidies may well lead to a suboptimal allocation of resources.

On exchange rate policy, I agree with the staff that there are signs that the exchange rate is still overvalued, in spite of the depreciation of the U.S. dollar to which the birr is pegged. It is gratifying that the authorities are prepared to study exchange rate policy. However, I regret that they prefer an internal study over a joint Ethiopian-Fund one. I hope this will not have the effect of delaying action into the distant future.

I note the authorities' views on the payments restrictions expressed in Mr. Abdallah's statement, although the argument that these restrictions would not be restrictive, but only an exercise of prudence in the face of difficult circumstances, is not convincing. I do not doubt the seriousness of the circumstances, and, although it may be just a matter of words, I think the only way these restrictions could help to conserve the scarce foreign exchange needed to ensure the availability of essential supplies would be by being, in fact, restrictive. I do not think it is realistic to remove the restrictions at this moment without further measures. I note that last year's approval of the existing restrictions was for a limited time period, during which it was expected that such further measures would be taken, thus ensuring the temporary character of the restrictions. However, such policy measures were not taken; consequently, the Fund should not approve the restrictions now. I strongly urge the authorities to prepare the ground for the removal of these payments restrictions, and I firmly believe that such action would be highly conducive to solving Ethiopia's very severe problems.

Mr. Finaish requested that the staff provide more information about the resettlement and villagization programs in Ethiopia, especially as they could not but have had an effect upon the agricultural sector, which, as many Directors had commented, was a crucial sector. There were also, of course, important human, political, and probably ethnic implications in the programs, which might be seen as falling outside the purview of the Fund. However, he would have particularly liked to have some assessment from the staff about the short- and long-term economic implications of the program.

Mr. Fogelholm remarked that in lieu of any real signs from the Ethiopian authorities of an inclination to remove the rigidities in the economy, particularly with respect to the price structure and the exchange system, or even to move in the direction of removing them, the question of approval of the restrictions on payments and transfers for current international transactions remained highly problematical. If the authorities intended to maintain their current pricing and exchange rate policies, obviously they would not be willing to move in the direction of eliminating the restrictions. On another matter, he wondered if the staff could estimate what the costs of the internal difficulties in Ethiopia had been, as it was evident, in his view, that these costs represented a substantial drag on the economy.

Mr. Vasudevan stated that he supported the arguments made by Mr. Abdallah, and that he had some questions about the economics of the staff report. First, the staff had stated that prices were sticky and that output would benefit from more incentives and further price liberalization. He had searched the report on recent economic developments for evidence that output in Ethiopia was price elastic, but had found little. Consequently, he wondered if the staff could show some tangible evidence that pricing policy was constraining output. In any case, he assumed that the staff was recommending price liberalization in a medium-term, and not a short-term, context. Second, Mr. Vasudevan noted that the staff had recommended that the currency be depreciated, but the background paper on the real effective exchange rate showed that there had already been a substantial depreciation in the exchange rate from 1985, and that, in particular, the rate in October 1987 was 93.9, against a rate in the first quarter of 1986 of 132.7. In his view, this represented quite a significant depreciation, and he wondered whether any further depreciation would really increase external competitiveness, given the market environment for Ethiopia's exports and its direction of trade.

Finally, he had noticed that the report showed that time deposits had declined in 1986, even though there had been a substantial increase in the interest rate, Mr. Vasudevan said. Thus, the savings rate in Ethiopia appeared to be income determined, and not interest rate determined; it was income elastic and relatively interest rate inelastic. He asked the staff to comment on whether that characteristic of the savings function, along with the low rate of inflation in Ethiopia, could be an argument in favor of an inflationary financing of growth, which might have the effect of also increasing the current relatively low savings rate, of about 3 1/2 or 4 percent.

Mr. Jiang said that because of Ethiopia's particularly difficult situation, he wished to support Mr. Abdallah's requests.

The staff representative from the Exchange and Trade Relations Department explained that the staff had recommended that the exchange restrictions be eliminated because it believed that they were not in the best interest of Ethiopia in the medium term. In not recommending approval of the restrictions on payments and transfers for current international transactions, the staff had been guided by the sense of the previous Article IV consultation discussion in July 1986, which was that unless there had been substantial progress in the adoption of adjustment measures necessary to eliminate the remaining restrictions, the Fund would not grant approval beyond December 1986; the hope that substantial progress would have been made on the negotiation of an arrangement under the structural adjustment facility by December 1986 had not materialized. In the absence of indications that the exchange measures would be temporary, the Fund did not generally grant approval.

The staff representative from the African Department said that the authorities had expressed an interest in additional external assistance during discussions with the staff in August 1987, in the form of another drawing from the compensatory financing facility, and had also made inquiries about the structural adjustment facility. However, the authorities had not yet followed up on those preliminary inquiries. When the Board approved the request for compensatory financing in early 1986, the staff had hoped that the authorities would pursue a structural adjustment arrangement, and during the consultation discussions in April 1986 the matter was considered further. Very preliminary negotiations for a program had begun at the end of 1986. At the time of the Interim Committee meetings in April 1987, the Ethiopian authorities once more indicated their interest in a structural adjustment arrangement, and again at the time of the Article IV consultations in August 1987. However, the authorities had not yet indicated how they would proceed with the staff's policy recommendations, so that the negotiations for a structural adjustment arrangement remained at a very preliminary stage.

On the extent to which the increase in suppliers' credits to Ethiopia in 1985 and 1986 was guaranteed by export credit agencies in the supplier country, the staff representative said that although there was some evidence that one or two countries had provided credit guarantees, the staff did not have detailed information but would look into the matter.

With respect to the public investment program, the staff representative went on, the Ethiopian authorities had prepared a Ten-Year Perspective Plan; however, subsequent developments had made it clear that it was too ambitious, and a new three-year subplan was drawn up, under which total fixed capital investment, including the World Bank's Peasant Agricultural Development Program, was about Br 5.7 billion. Of that amount, agriculture would receive about Br 1.4 billion. If the authorities intended to pursue a structural adjustment arrangement, the Fund and the Bank would need to take a much harder look at the subplan, and the ramifications of the public investment program.

No judgments had been made in the staff report about the economic implications of the resettlement and villagization program, the staff representative continued, as the staff had little expertise in that field. However, as had been widely acknowledged both inside and outside Ethiopia, the program had been costly, and the authorities had slowed down its implementation in order to consolidate what had been accomplished so far.

On another sensitive matter, the staff representative added, the staff had no detailed information about the costs of the insurgency in Ethiopia, a question that the authorities appeared reluctant to discuss.

Studies performed by the World Bank indicated that agricultural output in Ethiopia could be quite price elastic, the staff representative noted. There were many rigidities in the agricultural sector which reduced the incentive to farmers; for example, there were four different types of taxes affecting coffee, which was the most significant export: a 2 percent profit tax on all exports, including coffee; an export duty of Br 150 per ton; the coffee cess--a levy by the marketing board on the farmers for handling coffee--of about Br 6 per ton; and, finally, the coffee surtax of about 45 percent. The result was that farmers received only about 50 percent of the f.o.b price of coffee. The World Bank's studies of the agricultural sector had indicated that those taxes represented a major constraint on output. With respect to the exchange rate, in the period from 1976, when reliable price data became available, to mid-March 1985, the Ethiopian birr had appreciated in real effective terms by up to 91 percent, and had since depreciated, but not by enough to correct the substantial appreciation in the earlier period. Also, in concluding that the currency was overvalued, the staff had looked at a number of indices in addition to the real effective exchange rate index, including the trends in the domestic resource costs and in the private market rate of the birr, which had also indicated overvaluation.

In conclusion, the staff representative from the African Department observed that in assessing the exchange restrictions the staff had been well aware that they had enabled the authorities to build up reserves, thus also allowing them to remain current with their financial obligations. However, the restrictions had also introduced a number of distortions into the economy. They also needed to be seen in the context of the Board's instructions at the time of the consultation discussions in mid-1986, when the Board had approved the restrictions until December 1986 with the expectation that the authorities would take a number of actions. When a staff team visited Addis Ababa in December 1986, it was clear that the measures had not yet been taken. In August 1987, about 18 months after the Board had indicated the need to implement the appropriate policies so as to enable the removal of the restrictions, no actions had been taken. Furthermore, the authorities needed to take action in a number of other policy areas as well, such as producer prices, grain marketing and distribution, price controls, interest rates, and the exchange rate. Consequently, the staff had not believed that there was enough evidence to convince the Board to approve an extension of the restrictions.

Mr. Vasudevan remarked that, concerning the valuation of the currency, based on the information that was provided in the staff report, the real effective exchange rate indicator appeared to be a very important measure of the degree of the currency's depreciation. The depreciation shown with the base year as 1980 was quite significant. On the matter of domestic resource costs, in his experience it was difficult to draw firm conclusions based on domestic resource cost estimates without looking very closely into how the estimates were made. He suggested that in future the staff should show how the estimates had been derived when they were used to support a recommendation about the appropriate exchange rate. Interpretations of the accuracy and significance of domestic resource costs as an indicator of the appropriate exchange rate varied, so that when they were used to support an argument for devaluation, the methodology needed careful examination. Finally, on pricing policy, he hoped that the World Bank reports had addressed not only the export commodities, but other commodities as well; he also wondered whether taxes, transportation, marketing, and government subsidies had been taken into account in making price estimates in Ethiopia.

Mr. Finaish observed that despite the staff's promise to include more information about the resettlement and villagization program, there were only brief references to it in the staff's papers. It was an important program with important implications, and he asked if the Bank staff could provide more information, as the Fund staff could not.

The Acting Chairman said that the staff would take up the matter of the resettlement and villagization program in more detail in its next report, and would provide a more complete response at that time.

Mr. Abdallah observed that the Ethiopian economy had performed fairly well until the onset of another drought. Until that time the authorities had been interested in a structural adjustment arrangement, and believed that they might have been able to take action on the pricing system, as well as on other policy fronts. The authorities had seen the drawing they had made under the compensatory financing facility in 1985 as evidence of international cooperation, which had led them to begin some needed policy reforms. Another drawing from the compensatory financing facility which the authorities had considered making because of the drought would have exceeded 50 percent of quota, and thus would have required policy changes made necessary by the Fund's test of cooperation. The authorities believed that when a situation became as serious as Ethiopia's had become demands for policy changes were inappropriate; rather, aid should come first, with policy changes to follow, once the crisis had passed. Nevertheless, he believed that the authorities were still interested in a structural adjustment arrangement, despite the inauspicious timing.

The authorities were also still interested in making a general study of the exchange rate, as the staff had suggested, Mr. Abdallah continued. However, it would be more useful if the Fund were to undertake a study of regional exchange relationships rather than a general exchange rate study, in particular, between the birr and the Kenya shilling and the birr and the

Sudanese pound. A more important factor, in his view, was whether or not the birr was overvalued in relation to the currencies of those countries with which Ethiopia conducted most of its trading.

The Ethiopian authorities had in fact authorized his appeal, and that of some other Directors, for the mobilization of international assistance for Ethiopia, Mr. Abdallah stated. They were not expecting the Fund to actually initiate such a mobilization, but certainly the Fund could aid in the mobilization of opinion, which was what the authorities were hoping for; anything that could be done to mobilize a quick response to the very difficult situation in Ethiopia should be done, in his view. By not approving Ethiopia's exchange restrictions, the Fund would appear to be showing less understanding, at a time of need, than it had shown before, when the need was not as great.

In conclusion, Mr. Abdallah said that he would convey the comments of the Executive Directors to the Ethiopian authorities, including those on the issue of the resettlement and villagization program to which Mr. Finaish had drawn attention. However, he doubted that the authorities would engage in any further discussion on that very sensitive matter than they had already.

The Acting Chairman then made the following summing up:

> Directors observed that the strong economic recovery in 1985/86 and 1986/87 from the severely depressed drought conditions of 1984/85 had unfortunately appeared to have been temporary, and was already being jeopardized by the recurrence of drought, reportedly of the same severity as a few years ago. This underscored Ethiopia's dependence on highly concessional aid and humanitarian assistance to provide its population with basic human needs; several Directors called for a mobilization of international assistance for Ethiopia.
>
> Directors commented favorably on the authorities' cautious reserve management policies, which in the past have assisted Ethiopia in remaining current in the servicing of its external obligations. The importance of following prudent fiscal and monetary policies was stressed, and in that regard the prospective sharp widening of the fiscal deficit in 1987/88 was noted with serious concern. Directors also stressed the urgent need for the implementation of appropriate structural adjustment measures aimed at improving the current pattern of resource use, enhancing the prospects for economic growth and ensuring a viable external payments position. Directors urged the authorities to provide substantial incentives for production and exports by substantially raising producer prices, and by eliminating policy-induced distortions through the simplification of the existing complex agricultural marketing and grain distribution system. Directors also urged the authorities to improve the efficiency of public enterprises through the provision of greater financial and management

autonomy to these enterprises. Directors encouraged a substantive strengthening of the role of the private sector in the economy, and the implementation of measures aimed at encouraging domestic saving and investment.

Directors noted the difference of view between the authorities and the staff regarding the appropriate exchange rate policy, and urged that the proposed study to determine the appropriate stance be accelerated; indeed, some Directors encouraged the authorities to seek to work with the Fund on this study. The majority view was that there was continuing evidence of overvaluation of the exchange rate, and that it would be to Ethiopia's advantage to adopt a flexible exchange rate policy along with a flexible domestic pricing system.

It is expected that the next Article IV consultation discussions will take place on the standard 12-month cycle.

The Executive Board then took the following decision:

1. The Fund takes this decision relating to Ethiopia's exchange measures subject to Article VIII, Section 2(a), and in concluding the 1987 Article XIV consultation with Ethiopia, in the light of the 1987 Article IV consultation with Ethiopia conducted under Decision No. 5392-(77/63), adopted April 29, 1977, as amended (Surveillance over Exchange Rate Policies).

2. Ethiopia maintains restrictions on the making of payments and transfers for current international transactions as described in SM/87/288, which are subject to the Fund's approval under Article VIII, Section 2(a). The Fund urges the authorities to reduce reliance on exchange restrictions as soon as possible.

Decision No. 8765-(87/179), adopted
December 23, 1987

## DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/87/178 (12/21/87) and EBM/87/179 (12/23/87).

## 4. VENEZUELA - 1987 ARTICLE IV CONSULTATION - POSTPONEMENT

Notwithstanding the period of three months specified in Procedure II of the document entitled "Surveillance over Exchange Rate Policies" attached to Decision No. 5392-(77/63), adopted April 29, 1977, as amended, the Executive Board agrees to extend the period for completing the 1987 Article IV consultation with Venezuela to not later than January 6, 1988. (EBD/87/329, 12/18/87)

Decision No. 8766-(87/179), adopted
December 22, 1987

5. ASSISTANT TO EXECUTIVE DIRECTOR - EXTENSION OF OVERLAP PERIOD

The Executive Board approves the recommendation relating to the extension of the overlap period for the appointment of an Assistant to Executive Director as set forth in EBAP/87/279 (12/18/87).

Adopted December 22, 1987

6. ASSISTANT TO EXECUTIVE DIRECTOR

The Executive Board approves the appointment of an Assistant to Executive Director as set forth in EBAP/87/280 (12/18/87).

Adopted December 22, 1987

7. APPROVAL OF MINUTES

a. The minutes of Executive Board Meetings 87/91 and 87/92 are approved. (EBD/87/324, 12/15/87)

Adopted December 21, 1987

b. The minutes of Executive Board Meetings 87/93 through 87/95 are approved. (EBD/87/326, 12/16/87)

Adopted December 22, 1987

APPROVED: August 24, 1988

LEO VAN HOUTVEN
Secretary