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04

INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 86/45

3:00 p.m., March 12, 1986

J. de Larosière, Chairman

Executive Directors	Alternate Executive Directors
	Mawakani Samba
	J. K. Orleans-Lindsay, Temporary
	M. K. Bush
	M. Lundsager, Temporary
J. de Groote	G. Ercel, Temporary
M. Finaish	
H. Fujino	
G. Grosche	
Huang F.	
	J. Reddy, Temporary
	J. R. N. Almeida, Temporary
	M. Foot
	H. Fugmann
	O. Isleifsson, Temporary
	L. Leonard
E. I. M. Mtei	A. Abdallah
	C. A. Salinas, Temporary
	J. E. Suraisry
	J. E. Rodrīguez, Temporary
	S. de Forges
J. J. Polak	J. de Beaufort Wijnholds
	H.-S. Lee, Temporary
	R. Msadek, Temporary
	A. S. Jayawardena
S. Zecchini	N. Coumbis

L. Van Houtven, Secretary
J. K. Bungay. Assistant

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Also Present

IBRD: D. Dunn, Eastern, and Southern Africa Regional Office; R. Fernandes, Europe, Middle East and Northern Africa Regional Office. African Department: A. D. Ouattara, Director; C. Enweze, G. Kalinga. European Department: L. A. Whittome, Counsellor and Director; N. L. Happe, H. B. Junz, G. Szapary. Exchange and Trade Relations Department: J. O. Bonvicini, J. T. Boorman, E. H. Brau, G. Oliveros, P. J. Quirk, W. S. Tseng. External Relations Department: A. M. Abushadi. Fiscal Affairs Department: G. M. Bartoli, D. C. McDonald. IMF Institute: M. Huybrechts. Legal Department: F. P. Gianviti, Director; H. Elizalde, A. O. Liuksila, J. K. Oh, R. Munzberg. Middle Eastern Department: A. S. Shaalan, Director; P. Chabrier, Deputy Director; F. Drees, M. A. El-Erian, C. Sassanpour, E. M. Taha, G. Tomasson, M. Yaqub. Research Department: O. E. G. Johnson. Secretary's Department: J. W. Lang, Jr., Deputy Secretary. Treasurer's Department: J. E. Blalock, D. Berthet, J. C. Corr, M. F. Melhem. Personal Assistant to the Managing Director: R. M. G. Brown. Advisors to Executive Directors: W.-R. Bengs, S. M. Hassan, J.-C. Obame, A. Ouanes, I. Puro, D. C. Templeman. Assistants to Executive Directors: B. Bogdanovic, R. Fox, V. Govindarajan, H. Kobayashi, J. A. K. Munthali, A. H. Mustafa, V. Rousset, B. Tamami, H. van der Burg, Wang X.

1. YUGOSLAVIA - 1985 ARTICLE IV CONSULTATION; STAND-BY ARRANGEMENT - REVIEW AND MODIFICATION OF PERFORMANCE CRITERIA; AND ENHANCED SURVEILLANCE

The Executive Directors resumed from the previous meeting (EBM/86/44, 3/12/86) their consideration of the staff report for the 1985 Article IV consultation with Yugoslavia and the review under the stand-by arrangement for Yugoslavia, together with a request for a waiver of performance criteria and Yugoslavia's request for enhanced surveillance for the period May 16, 1986 through the end of 1991 (EBS/86/38, 2/19/86; Sup. 1, 3/7/86; and Cor. 1, 3/11/86). They also had before them a report on recent economic developments in Yugoslavia (SM/86/39, 2/27/86).

The staff representative from the World Bank said that an appraisal mission had gone to Yugoslavia in November 1985, in connection with a proposed structural adjustment loan, but it had not been completed. Discussions were continuing with the authorities on a number of points: the selection of investments in key infrastructure sectors, the adjustment of lending interest rates, the liberalization of the import regime, and the establishment of a foreign exchange allocation system that would ensure an effective trade liberalization process, in the sense that importers would have access to the foreign exchange required to import the liberalized commodities.

The Chairman made the following summing up:

Directors noted the continuation of a mixed and somewhat disappointing performance of the Yugoslav economy. Growth in 1985, barely positive, had remained considerably below target and inflation had accelerated. The balance of payments position had remained strong, even though the current account surplus in convertible currencies had been somewhat less than targeted. Solid external adjustment contrasted with slow and often inadequate internal structural change, many Directors emphasized.

All Executive Directors who spoke expressed great concern about the continued high rate of inflation in Yugoslavia. In their comments on the underlying causes, Directors stressed the need for constancy of policy and for improved cohesiveness of financial policies, as uncertainties and lack of mutual support in that area had undercut the effectiveness of individual policy measures. They also underlined the need for more resolute and sustained action to achieve durable improvement in the efficiency and cost effectiveness of the enterprise sector.

While monetary policy in 1985 had aimed at considerable stringency, the outcome clearly had been more expansionary than intended. Directors thus urged the authorities to strengthen control of credit expansion, both economy-wide and within the banking system. Many Directors noted the apparent role played by interenterprise credit in adding to the accommodation of inflation. They welcomed the additional measures being taken in 1986 to control such credit, namely, the limiting of guarantees of promissory notes to commercial banks and the planned provision by the commercial banks of attractive returns on the short-term deposits of the enterprises. But they also observed that, for those measures to have the desired effect, a more active liquidity policy on the part of the National Bank of Yugoslavia would be necessary.

Directors generally stressed the importance of interest rate policy for bringing down the rate of inflation and for ensuring an efficient allocation of resources in the economy. Many Directors deplored the lag in moving toward real positive interest rates in 1985, including the fact that lending rates were even more negative than deposit rates. In that regard, Directors welcomed the authorities' intention to lift the central bank's rates on selective credits effective April 1 to close to the discount rate and to raise, on the same date, the key three-month deposit rate to 73 percent, although some Directors questioned whether the latter increase was sufficient in the light of the recent acceleration in inflation. There was a consensus that the authorities should use interest rate policy more actively both as an anti-inflationary tool and as a means to facilitate a more efficient allocation of resources. An active interest rate policy, together with tight credit and fiscal policies, were seen to be critical for Yugoslavia, but a number of Directors expressed doubt whether the authorities had the necessary resolve to stick to the discipline that would be necessary to break inflation expectations.

Directors strongly encouraged the authorities to continue their efforts to improve financial discipline in the enterprise sector, in particular to implement the intention to close down nonviable operations, emphasizing the seriousness of the consequences of continued resource absorption by loss-making enterprises. They strongly encouraged the authorities to surface the true operating costs of the economy, to reduce the scope of subsidies, and at least to make their cost more explicit. They stressed the key impact on cost competitiveness in the economy of the various financial discipline efforts. However, many Directors believed that structural reform of the enterprise sector was proceeding at too slow a pace and that the remaining inefficiencies were an important underlying cause of inflation. As in the case of interest rate policy, several Directors urged that the efforts to strengthen enterprises' financial discipline not be relaxed following the expiration of the stand-by arrangement.

Directors highlighted the importance of maintaining the competitiveness of Yugoslav exports. Hence, an active exchange rate policy was considered essential given the authorities' ambitious medium-term targets for the current account surplus and debt reduction. Most Directors deplored the rigidities introduced in the recent changes in the foreign trade and exchange regimes, pointing out that they might reinforce the already pronounced tendency toward freezing of the current import and production patterns. A number of Directors expressed concerns regarding the economic costs of the extensive regulatory system and its attendant nontransparency.

Directors noted that the multiyear rescheduling of Yugoslavia's debt to commercial banks would shortly be finalized and supported the request for enhanced surveillance by the Fund that was to accompany that multiyear rescheduling arrangement (MYRA). They stressed that it was crucial that a policy course aiming at better internal balance continue to be pursued without wavering. It was important in that respect that the staff continue to assess the economic developments in Yugoslavia in a candid and broadly based fashion. With respect to the conditionality attached to the commercial bank, MYRA, many Directors noted that commercial banks had different objectives than official creditors and, therefore, also different requirements.

Finally, several Directors, noting the staff's new estimates of inventory accumulation, welcomed the authorities' moves toward undertaking a full review of the national income accounts methodology and statistics. Such steps were both important and urgent also in view of the start of enhanced surveillance.

It is expected that the next Article IV consultation with Yugoslavia will remain on the standard 12-month cycle.

The Executive Board then took the following decisions:

1985 Consultation

1. The Fund takes this decision relating to Yugoslavia's exchange measures subject to Article VIII, Section 2(a), and in concluding the 1985 Article XIV consultation with Yugoslavia, in the light of the 1985 Article IV consultation with Yugoslavia conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. As described in EBS/86/38 (2/19/86), the restrictions on the making of payments and transfers for current international transactions are maintained by Yugoslavia in accordance with Article XIV except that the restrictions evidenced by the

limitations on the availability of foreign exchange for travel and external payments arrears are subject to approval under Article VIII. In the circumstances of Yugoslavia, the Fund grants approval of the restriction on the availability of foreign exchange for travel until the completion of the next Article IV consultation or April 30, 1987, whichever is earlier, and of the restriction evidenced by external payments arrears until March 25, 1986.

Decision No. 8219-(86/45), adopted
March 12, 1986

Stand-By Arrangement - Review and
Modification of Performance Criteria

1. Yugoslavia has consulted with the Fund in accordance with paragraph 4 of the stand-by arrangement for Yugoslavia (EBS/85/85, Sup. 3, 5/1/85), paragraph 3(b) of Decision No. 8138-(85/172) of November 27, 1985, and the second paragraph of the letter dated September 30, 1985 and attached to the stand-by arrangement, in order (a) to review progress made in realizing the objectives of the program, (b) to reach understandings on policies and measures that the authorities of Yugoslavia will pursue for the remaining period of the stand-by arrangement, and (c) concerning the nonobservance by Yugoslavia of certain performance criteria as of December 31, 1985 and January 1, 1986, to reach understandings with the Fund regarding the circumstances in which purchases may be resumed by Yugoslavia under the stand-by arrangement.

2. The letter with annexed memorandum from the Governor of the National Bank of Yugoslavia and the Federal Secretary for Finance of Yugoslavia dated February 12, 1986 and the letter from the Governor of the National Bank of Yugoslavia and the Federal Secretary for Finance of Yugoslavia dated March 5, 1986 shall be attached to the stand-by arrangement for Yugoslavia, and the letters of March 15, 1985 and September 30, 1985, with annexed memorandum, shall be read as supplemented and modified by the letter with annexed memorandum of February 12, 1986, and the letter of March 5, 1986.

3. Yugoslavia will not make purchases under the stand-by arrangement that would increase the Fund's holdings of Yugoslavia's currency in the credit tranches beyond 25 percent of quota or increase the Fund's holdings of that currency resulting from purchases of borrowed resources beyond 12.5 percent of quota:

(a) During the period after April 29, 1986 if data at the end of the preceding period indicate that:

(i) the limits on net domestic assets of the banking system referred to in paragraph 8 of the memorandum annexed to the letter dated February 12, 1986 have not been observed; or

(ii) the target for the net convertible foreign reserves of the banking system referred to in paragraph 3 of the memorandum annexed to the letter dated February 12, 1986 or the limits on the disbursements of foreign debt referred to in paragraph 4 of the same memorandum have not been observed; or

(b) If the intention as regards interest rates on deposits as expressed in paragraph 9 of the memorandum annexed to the letter of February 12, 1986 and paragraph No. 2 of the letter of March 5, 1986 has not been carried out; or

(c) If the intention as regards interest rates charged by the National Bank of Yugoslavia as expressed in paragraph 9 of the memorandum annexed to the letter of February 12, 1986 and in paragraph No. 1 of the letter of March 5, 1986 has not been carried out; or

(d) During the period after March 25, 1986, if the intention as regards external payments arrears referred to in paragraph 4 of the memorandum annexed to the letter of February 12, 1986 has not been carried out.

4. The Fund finds that, in view of the letters of February 12, 1986 and March 5, 1986 no additional understandings are necessary regarding the circumstances in which further purchases may be made under the stand-by arrangement and decides, pursuant to paragraph 3(b) of Decision No. 8138-(85/172), adopted November 27, 1985, that the review provided for in that paragraph is completed.

Decision No. 8220-(86/45), adopted
March 12, 1986

Enhanced Surveillance

Yugoslavia has requested that the Fund provide enhanced surveillance for the period May 16, 1986 through 1991.

The Fund agrees to the request by Yugoslavia.

Decision No. 8221-(86/45), adopted
March 12, 1986

2. ENHANCED SURVEILLANCE - PROCEDURES FOR RELEASE OF STAFF REPORTS

The Chairman remarked that Yugoslavia's request for enhanced surveillance was the first to be dealt with under the policy agreed in principle at EBM/85/132 (9/4/85). Several procedures needed to be observed with respect to the release of staff reports during a period of enhanced surveillance by the Fund: the member could, if it so desired, transmit the annual and midyear consultation reports to the relevant creditor banks and other creditor institutions; the recipients would assure the member that the reports would not be used for any purposes other than those agreed with the member, and would be kept confidential; and the member would not transmit the reports to its creditor institutions earlier than two weeks after their issuance to members of the Executive Board.

The Executive Board then took the following decision:

When the Executive Board has approved a request by a member for consultations under the Fund's policy on enhanced surveillance, the annual and midyear consultation reports prepared by the Fund staff in accordance with that policy in respect of the member may be transmitted by the member to creditor banks and other creditor financial institutions party to the arrangements specified by the member in the request for consultations, on the understanding that the recipients of the reports have assured the member that the reports will not be used for any purpose other than those of the arrangements specified in the member's request to the Fund and will be kept confidential; and that the reports shall not be transmitted by the member earlier than two weeks after their circulation to members of the Executive Board.

Decision No. 8222-(86/45), adopted
March 12, 1986

3. SUDAN - 1985 ARTICLE IV CONSULTATION

The Executive Directors considered the staff report for the 1985 Article IV consultation with Sudan (SM/86/33, 2/19/86). They also had before them a report on recent economic developments in Sudan (SM/86/38, 2/26/86).

The staff representative made the following statement:

Since the issuance of the Article IV consultation reports (SM/86/33 and SM/86/38), the staff has received additional information, summarized below, on economic developments and on the implementation of policies.

Directors will recall, with respect to the budget for 1985/86, that the authorities had announced at the end of January 1986 the implementation of additional revenue measures which, according to their estimates at that time, would yield some LSd 140 million in the remainder of the current fiscal year ending June 30, 1986. These measures, the entry into effect of which was delayed by a month, include: sale of 25-30 percent of available sugar supplies to consumers at a price of LSd 0.60 per pound, as compared to the price for rationed entitlements of LSd 0.30; an increase in the price of gas oil from LSd 2.75 to LSd 3.50 per gallon, thereby reversing the price cut effected in July 1985, and sale of 25 percent of available benzine at prices of LSd 10 per gallon and LSd 11 per gallon for regular and super, respectively, as compared to the prevailing prices for rationed benzine of LSd 7.50 and LSd 8.00. The authorities also decided to increase, by 10 percent to LSd 610 per ton, the price paid to some factories by the public sector sugar distributing agency without effecting a further adjustment in the retail price; this will result in a loss of some LSd 10 million. The combined impact of all these measures is estimated to be about LSd 135 million in the remainder of the current fiscal year.

The authorities are also reported to be considering other budgetary measures, including expenditure cuts of 10 percent in selected items of the budgets of the Government and public corporations and introduction of a compulsory savings scheme under which all employees in the private and public sectors earning more than LSd 150 per month would contribute a certain portion of their basic salary, to be repaid in April 1987.

On monetary developments preliminary data for the four-month period ended January 1986 indicate that Sudan's money supply grew by an estimated 12 percent of the money stock as of end-September 1985, as compared to the 20 percent target established in October for the 12-month period ending September 1986. Government borrowing amounted to some LSd 345 million during this period, compared to the October target of LSd 200 million for the fiscal year as a whole. At the same time, recourse to bank credit by public entities amounted to about LSd 210 million, significantly above the indicative target of LSd 12 million for the quarter ended December 1985 and LSd 189 million for the six-month period ending March 1986.

As indicated in the staff report (SM/86/33) a committee of representatives of commercial banks was established at the end of January 1986 to determine the exchange rate in the commercial bank market. Initially the rate had been kept unchanged at US$1 = LSd 3.30/3.35, well below the "black market" rate, which then stood at about US$1 = LSd 5.00. The flow of remittances to banks at this rate was negligible and, in an attempt to provide resources for import financing, the authorities had to divert foreign exchange from the official market to the commercial banks. However, on February 26, 1986 the commercial bank rate was depreciated to US$1 = LSd 4.25/4.30 compared with the prevailing black market rate of about US$1 = LSd 4.80. While the depreciation of the commercial bank rate is a significant move in the right direction, the new rate may still be inadequate to attract resources to the commercial bank market while, at the same time, continued diversion of foreign exchange from the official market to the commercial bank market will aggravate the existing imbalance in the official market.

Sudan has made payments to the Fund since January 31, 1986 and, as a result, its arrears amounted to SDR 242 million as of March 7, 1986.

Extending his remarks, the staff representative from the Middle Eastern Department informed the Executive Board that the latest calculation of the real effective exchange rate for the Sudanese pound, made in the context of the information notice system, indicated that by January 1986, the pound had depreciated in real effective terms by an estimated 10.7 percent since May 1985, when developments in the exchange rate for the Sudanese pound had previously been brought to the attention of the Executive Board. As the calculation had been completed only on the preceding day, there had not been enough time to issue an information notice before the Executive Board meeting.

Mr. Mtei made the following statement:

Apart from the Article IV consultation reports, the Executive Board has been kept fully informed by the staff on developments in the Sudanese economy and the adjustment efforts of the authorities. It is well known that the economy of Sudan has experienced exceptionally difficult economic and financial conditions in recent years characterized by a sharp deterioration in the external payments position, severe shortage of foreign exchange, buildup of external payments arrears, declining output, widening fiscal deficit, and high inflation. Economic activity declined for the third successive year in 1984/85 with real GDP falling by 7 percent.

As the details of these developments are well known to Directors, and are fully described in the staff reports, instead of reiterating details and the efforts that the authorities have made to address the situation, I would prefer to focus on some of the fundamental issues which have continued to overshadow developments in the Sudanese economy and on which I would like Directors to focus attention in today's discussion.

Perhaps I should start by stressing the fact that against the background of a difficult economic and financial situation the present Government in Sudan, since it assumed office in April, 1985 has demonstrated quite convincingly, by implementing wide-ranging adjustment measures, that not only does it wish to cooperate with the Fund in finding solutions to Sudan's economic problems, but that it is prepared also to do what is necessary in order to reverse the deterioration in the economy and improve the situation. However, the outcome of the authorities' efforts has been constrained by a number of exogenous elements, including natural factors such as the prolonged drought causing famine and an influx of refugees from neighboring countries, external factors such as the disruption and decline of foreign assistance, the security situation in some parts of the country, and social and political tensions limiting the scope of what practically can be done. Directors should note that under such circumstances, no matter what the authorities' intentions and commitments are, progress is expected to be gradual and slow and adjustment can be achieved only over an extended period of time.

A fundamental fact of the economic situation in Sudan is that the overhang of the external debt dominates the scene and makes policy decisions very difficult. As a matter of fact, there is no feasible means of domestic adjustment which by itself would make it possible for Sudan to reverse the situation in a short period of time, with only normal aid flows and commitments from traditional donors. With a huge projected debt service ratio of more than 355 percent in 1985/86 and outstanding arrears equal to 20 percent of its GDP and three times its estimated export receipts, the formulation of elements of a meaningful domestic adjustment effort would be possible only with abnormal external assistance. To use the staff's own words in a memorandum to the Government of Sudan on economic policies last year "...reliance on domestic effort alone would require compression of imports and real income to a level that would exert a depressive effect on domestic output and investment, possibly resulting in a downward spiraling of economic activity. Moreover, the domestic effort to attain the outcome was found to be of such a daunting magnitude that the mission did not find it realistic. For example, it would have involved a reduction in average real incomes of about 50 percent, which in the mission's judgment would have exerted extremely undesirable consequences for the long-term recovery of the economy, in addition to being politically and socially unacceptable."

Therefore, it is my belief that to be practical, any future adjustment effort should focus first, and as an integral part of the program, on a realistic solution to Sudan's external debt problem. Such a solution would necessitate conversion of the bulk of Sudan's official debt into grants and rescheduling of private debt over an extended period of time and on terms and conditions consistent with the country's ability to service it while at the same time facilitating some economic growth and improvement in domestic living conditions. In this regard I would reiterate the call by the G-24 Ministers in their communiqué following their meeting in Buenos Aires, Argentina last week on the treatment of the debt of low-income countries. Such an approach would call for concerted international effort on the part of Sudan's donors and creditors and multilateral institutions to support domestic adjustment measures. Perhaps the Fund and the World Bank together should take a lead on this.

So far the strategy that has been followed by the Fund and Sudan's donors and creditors has concentrated on asking Sudan to prepare and implement a comprehensive and strong adjustment package and insisting on prior actions before external support could be provided. This strategy, as we all know, has not worked, not because of the lack of commitment on the part of the authorities as many would like to think but mainly because the approach itself ignored the fact that finance and adjustment go hand in hand, and in many cases they become a prerequisite for the availability of financing the successful implementation of some adjustment measures. I therefore believe that a better approach would be for the international community to make appropriate levels of financing readily available for the authorities to mitigate the unacceptably high cost of such implementation and not to wait to provide financial support only after full implementation of all policy measures.

The structural nature of the economic and financial problems facing Sudan and the depth and magnitude of the imbalances are such that the situation cannot be reversed in a period of one year. An unrealistic pace of adjustment in an effort to achieve clear progress over a short period would only be counterproductive, resulting in a disruption of adjustment efforts in the face of mounting social and political pressures. Perhaps it is not necessary to quote evidence of this as we all recall what happened in Sudan last April. For an adjustment effort to be successful it is important to press for what is feasible under the prevailing circumstances. Problems accumulated over decades--as in the case of Sudan because of both external factors and inappropriate domestic policies--can be resolved only gradually and over a number of years and with substantial external support to sustain domestic efforts. Our future efforts to address the problems of the Sudanese economy should not lose sight of this fundamental fact.

There are two policy issues on which the staff mention differences of opinion between them and the authorities. The first is the devaluation of the Sudanese currency. I might point out that the prevailing public perception in Sudan with regard to the devaluation of the national currency may have an important bearing on the authorities' views on the issue. It is a fact that in the mind of the average Sudanese, devaluation of the Sudanese pound, whether rightly or wrongly, has been seen as a cause of all the economic deterioration that took place in the country since 1978, not as an effect. This is why even government officials and policymakers argue that the Sudanese pound has been devalued six times in the last seven years without any positive results. The only certain result, the argument continues, has been the sharp and spiraling rise in domestic prices.

Against this background the authorities have held the view that while they agree to the maintenance of a flexible policy to correct the overvaluation of the exchange rate and to the objective of unification of the exchange rates, they believe that this should be achieved gradually and after preparation of a conducive environment to ensure success. If the prerequisites for effective use of devaluation as an economic policy tool do not exist, it will become a futile exercise. Moreover, the issue of devaluation in many developing countries--and Sudan is the best example--has become a political issue and related for many citizens to national sovereignty and pride. These are realities which should be taken into consideration when prescribing corrective measures or advising on adjustment policies. A degree of flexibility becomes necessary to reach understanding with national authorities; we need not be dogmatic or mechanistic in our effort to help member countries find solutions to their economic problems. It is important to stress that a successful adjustment would always require the support and backing of the public.

Another area of difference is related to interest rate policy. The authorities believe that the theoretical relationship between interest rates and the level of savings does not necessarily hold in the case of Sudan because of a number of institutional, social, religious, and economic factors. As a result, interest rates have a limited scope to play as a policy instrument to mobilize and allocate resources in Sudan. These factors include nonconducive social and religious beliefs, underdeveloped banking network and habits, a low interest elasticity of savings and investment, which are constrained by the low income level and lack of necessary infrastructure, and the relatively large nonmonetized sector of the economy. They understand the importance of positive returns to savers and investors in promoting a more efficient resource allocation. However, they believe that savings mobilization and better utilization of funds would require more than mere increases in interest rates. Development of banking habits and spreading of bank branches in rural areas and introduction of savings instruments that are socially and religiously acceptable to people are equally important. Here again, I would call for flexibility and an open-minded approach without any prejudice as to the character of the existing financial intermediation and policy instruments used as far as they could lead to the same objective.

It is to be noted that the authorities and the staff are in complete agreement in all other policy areas, including effective demand management, relaxation of price and profit controls, institutional reform and stability, improvement of the performance of the public enterprises, and provision of adequate incentive for producers. The authorities have also gone a long way in implementing many of the agreed policies. The recent measures, including increases in sugar and oil prices, expenditure cuts, introduction of a compulsory saving scheme, and the adjustment in the commercial bank exchange rate are a clear indication of the authorities' commitment to continue with their adjustment efforts.

A major difficulty facing the Sudanese authorities, and about which they are deeply concerned, is the regrettable situation of arrears to the Fund. On several occasions I have emphasized to this Board the authorities' commitment to clear their arrears as soon as possible and remain current in their obligations, and I would like to reiterate that commitment today. They consider the Board's decision to declare Sudan ineligible on February 3, 1986 as a most unfortunate development which they had tried to avoid by all possible means. Nevertheless, the authorities would like to assure the Board that despite the adverse impact of the decision on Sudan's efforts to secure an early settlement of the arrears, it has neither affected their commitment to discharge the arrears as early as possible nor their willingness to continue their cooperation with the Fund in finding solutions to their problems. However, they would urge the Executive Board and Fund management to show flexibility and understand the exceptional hardships facing Sudan. They would urge Directors to view with sympathy and pragmatism the case of Sudan in their evaluation of the situation.

On a personal note, I would like to repeat that the case of Sudan's arrears to the Fund would require an innovative approach as full settlement of the existing level of arrears, considering the fast rate at which they are accumulating is well beyond what Sudan can effectively meet without substantial support of the donors and the international community.

My main objective in limiting my statement to the above fundamental issues rather than following the normal approach of describing recent developments in the Sudanese economy and the adjustment efforts of the authorities is to draw the attention of Directors to the fact that the case we are considering today is especially difficult and the strategy that has been adopted so far has not worked, mainly because of the prevalence of special circumstances which, in my view, call for a new, bold, and creative approach on the part of the Fund, other multilateral institutions and Sudan's donors and creditors, as well as a strong will and commitment on the part of the Sudanese authorities to adopt a comprehensive adjustment program capable of addressing the deep-rooted economic problems. The country is now in the process of elections which are scheduled for April 1-12, 1986 and the newly elected government is expected to assume office in May. The assumption of office of the new Government should provide an opportunity to resume a more comprehensive and vigorous effort to help Sudan address its economic problems and eliminate its arrears to the Fund.

Mr. Suraisry said that the Sudanese economy continued to face formidable problems--GDP had declined by about 13 percent in the past three years, the balance of payments and fiscal operations were suffering from severe imbalances, and external arrears had risen to 20 percent of GDP. To a large extent, those problems were the result of the inappropriate economic policies that had been maintained for several years. Adjustment had been postponed, and even when some adjustment measures had been taken, they had often lacked continuity and comprehensiveness. Unfortunately, that type of on-and-off adjustment policy had been accompanied by extremely adverse exogenous factors: problems in the south, the refugee problem, the long drought, and last but not least, the famine.

Despite the grave situation in Sudan, a number of positive developments had occurred recently, Mr. Suraisry continued. A new Government had taken office in the past year, the weather conditions had improved, the international community had become sympathetic to Sudan's problems, and confidence in the new Government by expatriate Sudanese had grown. The authorities should take advantage of those developments by adopting policies that would lay the basis for sustained improvement in the economy. Any further delay of those policies would probably lead to an erosion of confidence in the new Government and make the task more difficult. The authorities had adopted a number of measures to ameliorate the economic situation. Measures had been introduced to halt the deterioration in the fiscal operations, to increase the incentives for output, and to strengthen the external position. However, considerable efforts were still needed. As the experience of Sudan had shown, and given the magnitude of its difficulties, a piecemeal approach to the country's problems would not be sufficient.

The staff had outlined comprehensively the policy measures that were needed to put the Sudanese economy back on track, Mr. Suraisry noted. Obviously, a comprehensive adjustment plan that entailed demand management and supply-side measures was urgently needed to deal with the country's immediate problems and lay the foundation for a viable balance of payments position.

Both fiscal and monetary developments in the past two years had greatly weakened the financial side of the economy, aggravating the already difficult economic position, Mr. Suraisry considered. He was concerned that even with the recent measures, budgetary revenue was projected to be only one half of total expenditure. That highlighted the need, not only for additional new revenue measures in the context of a financial reform, but also for firm demand management policies so as to improve the fiscal position and reduce the heavy dependence on bank borrowing. Such bank borrowing made it difficult to strike a balance between restricting the rate of monetary expansion to reduce the already high rate of inflation and ensuring adequate credit for the productive sectors.

The supply-side measures should be an important component of any plan for tackling the problems of the Sudanese economy, as they were essential to restore an appropriate price structure and thus to stimulate domestic output, particularly in agriculture, Mr. Suraisry commented. The favorable weather conditions experienced in the past year had provided some room for maneuver, and the authorities should capitalize on them by moving toward a price structure that reflected costs, particularly in the agricultural sector. Such a move should encourage private sector participation in the development effort, which required special attention. The authorities needed to remove price and profit controls, because those controls undoubtedly complicated domestic investment decisions and discouraged private sector activity, leading to an increased scarcity of goods, with obvious implications for the budget and the rate of inflation.

Stimulating domestic production was also important in view of the difficult debt problem facing the authorities, Mr. Suraisry went on. Adequate attention should be given to the need for increasing exports, and to that end, an appropriate exchange rate and the gradual liberalization of the exchange and payments system were essential.

The task ahead of the Sudanese authorities was so difficult that even if they implemented all of the recommended measures, serious problems would still remain, Mr. Suraisry observed. The assistance of the international community should therefore be an integral part of the plan to restore the economic balance of Sudan. In particular, the active participation of the Fund, the World Bank, and other international financial institutions was critical, but unfortunately, it had been complicated by Sudan's overdue financial obligations, which continued to rise. Sudan had missed a good opportunity to settle its arrears to the Fund and consequently to benefit from the financial assistance that it badly needed. However, that was history, and what was important was to act quickly to pave the way for prompt settlement of those arrears before that became too difficult and the economic problems insurmountable. Finally, he supported the proposed decision.

Mr. Foot observed that some positive factors had finally emerged in Sudan, notably the sharp improvement in agricultural output in the current year. Together with the known willingness of certain friendly governments to give generous amounts of aid, those factors could provide a far from hopeless backdrop to genuine efforts at economic adjustment. What was depressing, however, was that there still seemed to be inadequate realization on the part of the Sudanese Government that major adjustment across the board was necessary and that every month of delay made the task of adjustment more and more difficult, particularly with respect to the external position. It appeared that the authorities were implementing--but only in part--some of the measures thought vital by the staff. For example, substantial fiscal retrenchment had been necessary, and Sudan had announced measures that went part of the way to make the required adjustment. The increase in producer prices was essential. It would be helpful to have the staff's confirmation that present producer prices--given a realistic assumption about the exchange rate--did actually provide adequate incentives. He wondered why, in the face of good crops and adequate producer prices, the Government felt constrained to increase land and water charges by only half the amount judged necessary by the Fund and the World Bank. Unfortunately, it was not clear that the measures taken to date would be actively carried through or that they would form part of the stable, rational environment necessary to restore the Sudanese economy. In particular, few of the measures seemed to offer much prospect of reducing the distortions found everywhere in the economy that prevented the sensible allocation of economic resources.

The staff's view that a major devaluation was necessary, together with measures to ensure eventual unification of the exchange rate, had been endorsed by the Board on several occasions, Mr. Foot recalled. However, the authorities had revised their previous approach in a way that left the official exchange rate at roughly half the parallel market rate, had initially left the commercial bank exchange rate wholly out of line with that of the parallel market, and still involved major bureaucratic and other controls on foreign exchange transactions. Although a significant depreciation of the commercial bank rate had now been permitted, other controls remained, and the official rate continued to be as unrealistic as ever. There had been a number of changes in the fiscal area. He wondered what the current state of islamization of the banking system was, and how able it was--within the present rules under which it operated--to help underpin the recovery efforts of Sudan.

There was little in recent developments, or in the continued overshooting of government borrowing and its recourse to bank credit, that augured well for the future, Mr. Foot concluded. It was important to remember that ineligibility was not the end of the road for a Fund member and that the Fund remained willing to provide what assistance it could. However, nothing could be achieved unless the Sudanese Government had an adequate perception of its problems and demonstrated its willingness to undertake actions across the entire range of policies in order to make a genuine adjustment effort. Finally, he supported the proposed decision.

Mr. Finaish observed that the performance of the Sudanese economy had deteriorated sharply in the 1970s and had remained generally below its potential. A number of factors had contributed to that situation and to the failure of economic adjustment efforts undertaken in the context of several Fund-supported programs: economic mismanagement, protracted drought, the sizable influx of refugees from neighboring countries, disruptions and shortfalls in foreign aid, internal security problems, social tensions, and political instability. Against that background, economic performance had recently suffered further setbacks as manifested by negative real growth, increased inflationary pressure, and further worsening of the financial situation in terms of both fiscal and monetary indicators. Consequently, the external payments position had also continued to deteriorate, reflecting severe shortages of foreign exchange and a buildup of external payments arrears.

There was no doubt that Sudan's difficult economic situation had already entailed enormous costs in both economic and human terms, Mr. Finaish stated. One manifestation was the decline in overall economic activity for the third successive year in 1984/85, with real GDP estimated to have fallen by 7 percent; for the three-year period as a whole, the decline in real GDP had amounted to 13 percent. If allowance was included for increases in the population over the same period, the result would be a reduction of approximately one fifth in real GDP on a per capita basis. Another indication of the seriousness of Sudan's difficulties was the famine conditions that both Sudanese nationals and about two million refugees from neighboring countries had suffered. There were still other indicators of economic hardships, but they were hardly needed to portray the urgency with which Sudan's problems had to be tackled effectively.

The staff had rightly pointed out that Sudan's economic and financial problems were structural in nature and that their resolution would require early implementation of a medium-term strategy designed to expand output, contain demand, and change relative prices so as to encourage exports and import substitution, Mr. Finaish considered. Sudan's present Government, though transitional and constrained by limited room for maneuver, had nevertheless accorded high priority to addressing the country's economic difficulties, including the arrears to the Fund. To that end, the authorities had worked closely with the Fund and had adopted a number of significant adjustment measures, in preparation for the adoption of a Fund-supported economic program. When Sudan had recently been declared ineligible to use the Fund's resources, he and other Directors had expressed concern that such a step might prove harmful to cooperation between the Fund and Sudan. The Fund could have shown greater understanding of the particular circumstances of Sudan without necessarily compromising any of the principles governing Fund/member relations.

The uncertainties and waste of resources arising from political and social instability as well as civil unrest should be alleviated to establish an environment conducive to the successful implementation of a major policy package of economic adjustment such as the one recommended for Sudan, Mr. Finaish went on. Some modest progress had already been achieved toward that end since the present Government had taken office in April 1985. However, further progress awaited the establishment of a new Government after the elections scheduled for April 1986.

Notwithstanding the importance attached to the technical aspects of the design and pace of economic adjustment, those considerations should be carefully balanced against the risk of giving rise to social and political upheavals in Sudan, Mr. Finaish added. Putting Sudan back on the path of economic adjustment and toward economic recovery should take precedence over the magnitude of the initial adjustment, the pace of adjustment, and/or the particular choice of adjustment measures. In that context, Mr. Mtei had made useful remarks with respect to the interest rate and exchange rate adjustments that had been recommended by the Fund.

A major obstacle to the immediate undertaking of economic adjustment in Sudan was the availability of adequate finance consistent with what could be considered a realistic pace of adjustment, Mr. Finaish suggested. The magnitude of debt relief and aid flows needed to help Sudan restore sustainable growth and balance of payments viability was large indeed. Less than full utilization of Sudan's good economic potential would ultimately be more costly to both Sudan and its creditors.

Countries in his constituency, as well as Arab development funds, had been a major source of financial support for Sudan over the years, even though that fact had not received adequate attention in the staff report, Mr. Finaish pointed out. Apart from substantial grants, loans from official Arab creditors accounted for some 45 percent of Sudan's outstanding debt from official sources. Recognizing that the alleviation of Sudan's debt servicing pressures was critical for the country's adjustment efforts, those creditors had been formulating approaches to deal with the debt servicing problems. Some creditors--specifically, the Arab development funds--had been unable to reschedule Sudan's debt because of provisions of their charters; however, those institutions, which had ceased disbursements to Sudan because of its outstanding arrears, had sought alternative means of restoring a normal financial relationship. In particular, a number of Arab funds had arranged for bridge financing from regional banks to settle those arrears, and immediately thereafter those groups had provided Sudan with resources for the local cost component of some projects amounting to about $150 million. Such incremental foreign exchange, made available up front to the authorities, had provided the necessary resources to repay the bridge loan. As a result of that innovative approach, the funds and Sudan were in a position to resume a normal financial relationship without violating the charters of the institutions or placing undue pressures on the Sudanese economy. Additional project financing extended to Sudan from Arab development funds was expected to be on the order of $150 million over the next year or so.

Although the problems facing Sudan were exceptionally difficult, there was no alternative but to persevere in the efforts to find practical, effective solutions, Mr. Finaish advised. To be sure, the Sudanese authorities would have to take decisions that might be quite painful. However, what was critical was sufficient external support to enable the authorities to keep the social and political costs of adjustment within tolerable levels. In that context, sight should not be lost of the limitations on the new Government that was trying not only to deal with the economic inheritance from the previous regime but also to re-establish democratic institutions in the country and encourage wide participation in the decision-making process.

Mr. Mawakani remarked that the economic and financial situation of Sudan, which the Executive Board had reviewed extensively over the past 12 months, continued to be worrying. Indeed, the economy had deteriorated further in 1984/85, with real GDP having decreased for the third consecutive year. That deterioration had been accompanied by severe inflationary pressures, large internal and external imbalances, and a high level of external indebtedness, the servicing of which had become increasingly unsustainable burden. The reasons for the deteriorating situation were well known. Natural and external factors--such as the prolonged drought, particularly severe in 1984/85, that had led to widespread famine, and the disruption in the availability of foreign aid--had been instrumental in Sudan's poor performance, but internal factors such as inadequate economic and financial management and the failure to implement the required adjustment policies had also contributed to the deterioration of the economic situation. To come to grips with the various economic and financial difficulties confronting Sudan, the authorities should implement corrective measures without delay in the context of a medium-term recovery program that could address the immediate problems and lay the foundation for a viable fiscal and external position.

Like many other African countries, Sudan's economic and financial problems were of a structural nature and thus needed to be tackled in a medium-term context, Mr. Mawakani noted. Such a policy framework should emphasize the need for implementing supply-side measures aimed at expanding output. In that connection, he was pleased that in the agricultural sector, the Government of Sudan and was currently implementing pricing policies and other incentive measures which, combined with the current favorable weather conditions, were expected to increase agricultural output by 33 percent in 1985/86. Those commendable policies, especially the priority being given to the provision of essential agricultural inputs, should be pursued. Furthermore, given the importance of the cotton sector, the financial position of the marketing company should be strengthened.

The Government of Sudan intended to initiate structural reforms designed to increase industrial production, Mr. Mawakani mentioned. If effectively implemented, those reforms could go a long way in solving the problem of the unsatisfactory performance of the manufacturing sector and the public enterprises. The ongoing involvement of the World Bank in that important exercise was welcome. He urged the authorities to consider measures that would help to ease the excessive controls that had been hampering the efficient operation of the manufacturing sector.

Within the context of the 1985/86 budget, the authorities were making significant efforts to improve the management of the public finances and the overall fiscal position, Mr. Mawakani considered. Those efforts were mainly directed at expenditure restraint and control, but it was equally important that additional measures be taken to strengthen the revenue position. To that end, the authorities should broaden the revenue base and make the elasticity of taxes more responsive. Given the ongoing reforms in the parastatal sector, the contribution of the public enterprises to the budget should increase with their improved financial performance.

The monetary policy pursued thus far had been expansionary, and had led to inflationary pressures in the economy, Mr. Mawakani continued. Monetary expansion and credit had mainly reflected the deterioration of the budgetary position. To reduce the internal financial imbalances, the authorities should control credit allocation to the private and public sectors to help promote activities essential for Sudan's economic recovery and sustained medium-term growth. The authorities should also ensure the stability of the institutional mechanism for mobilizing domestic financial resources.

It was worrying to note that Sudan was so far from achieving a viable balance of payments position, Mr. Mawakani added. However, Sudan's balance of payments position could improve somewhat over the medium term, depending on certain conditions--notably, climate and external capital inflows--that were beyond the control of the authorities. However, other equally important conditions were within the authorities' reach, as they depended on their commitment to implement policies. The authorities should abandon their stop-and-go approach and, without delay, start to implement a comprehensive package of adjustment policies that would ensure a smooth pace of adjustment. Nonetheless, it was important to remember that in the absence of substantial international financial support, the prospects for an improvement in Sudan's economic and financial performance would remain highly uncertain.

Mr. Leonard said that it would take dedicated effort and several years for Sudan's economy to recover from its current dilapidated state and to approach a balanced operation. The authorities would have to initiate that effort by accepting a policy framework along the lines proposed by the staff and by creating conditions to attract the help required from the international financial community, the Fund, and the World Bank. Sudan's situation was fairly bleak, although there were some glimmers of hope. With the cessation of the drought and the provision of international aid, the famine conditions that the country faced in 1984/85 had been relieved, and the authorities could give more attention to other pressing concerns. Fortunately, as a result of better weather, there were prospects of improved agricultural production and higher exports of cotton and other merchandise. The new Government recognized the need for radical measures to tackle Sudan's economic problems, and it seemed to have the required resolve to initiate them. Furthermore, the staff and the authorities had identified a policymaking path, albeit precarious, through the present difficulties toward greater medium-term balance.

The authorities were making progress in realizing the potential of the agricultural sector, and were rightly trying to ensure adequate prices that would encourage production of several crops, Mr. Leonard remarked. However, the 1985/86 price stipulated for long- and medium-staple cotton, combined with the present level of the exchange rate for the Sudanese pound, entailed a "loss" for the cotton marketing company, a loss that could be overcome if the authorities adopted a more flexible and realistic exchange rate policy. He hoped that in spite of the sociopolitical difficulties involved, the authorities would move toward full recovery of costs in the major agricultural schemes. Nevertheless, the authorities had rightly noted the need to supplement the pricing policy with other action to encourage agricultural production. Adequate availability of spare parts, the rehabilitation of agricultural projects, and improvements in infrastructure were all needed, but would not be forthcoming without debt relief and foreign aid from the international community. At the same time, the authorities had to realize that the way must be cleared for such external aid, and that they had a part to play in clearing it.

To promote supply-side policies generally, and specifically in the manufacturing sector, a relaxation of price and profit controls would be beneficial, Mr. Leonard suggested. It was therefore regrettable that the authorities had acted as recently as January 1986 to increase economic regulation, in spite of their apparent awareness of the shortcomings of the present system.

The budgetary prospects for 1985/86 were not good: even on the basis of the revised budgetary figures, which took account of the end-January revenue measures, the likely outturn was a further large deficit that would entail extensive domestic borrowing, continued failure to meet external debt commitments, and a further accrual of external payments arrears, Mr. Leonard stated. It was of the greatest importance that the authorities seek to avoid such an outcome, with its consequences both for the domestic monetary situation and for Sudan's external financial standing. In that regard, his authorities regarded the staff's recommendations on further revenue measures as cogent and fully justified by the financial position of the Government. Accordingly, they urged the Government of Sudan to resume--along with the Fund--the search for a package of immediate and medium-term policy measures that would bring the economy back to a reasonable degree of balance and provide a basis on which the international financial community could act.

The fiscal imbalance and the inadequacy of the authorities' measures to deal with it were at the root of the policy problems that had contributed to the woeful deterioration in the economic performance of Sudan, Mr. Leonard considered. Other policy deficiencies in the monetary and external areas stemmed from the same root, and needed to be rectified by such actions as curbing the rate of growth of monetary expansion, promotion of private savings and investment, and adoption of a realistic and flexible approach to the management of the exchange rate, including early unification of the existing rates. The attention of the authorities to those issues was urgently needed, even more so in view of the several factors outside the sphere of economic management, which, if they proved to be unfavorable, would greatly exacerbate the problems of economic recovery.

He believed that there had been policy failures, but fully appreciated to what extent exogenous elements had disrupted the economy of Sudan, Mr. Leonard pointed out. He also recognized that it would take time and extraordinary effort by the international financial community to remedy the situation. Mr. Mtei's confirmation that the Sudanese authorities wished to cooperate with the Fund in finding solutions to their problems had provided a welcome counterpart to the readiness already shown by the Fund, the World Bank, and donor countries to work in the same direction.

Although Mr. Mtei had indicated that devaluation of the Sudanese pound was a political issue related to national sovereignty and pride, and therefore represented difficulty for the authorities, it was encouraging that they had already depreciated the commercial bank rate, Mr. Leonard commented. He hoped that more could be done soon, and that in the meantime, a vigorous effort would be made to prepare the financial environment and the public mind. The necessary interest rate policy also posed problems for the authorities. He understood that savings mobilization and better utilization of funds required more than mere increases in interest rates. However, that did not mean that action on interest rates should be ignored, pending action of a more structural kind that might be required to make changes in rates more fully effective.

Mr. Grosche remarked that Sudan's economic difficulties had been discussed on several occasions in recent months, and unfortunately, nothing fundamentally new had emerged from the latest staff reports to inspire hope that the economic policymakers were taking things firmly in hand. Moreover, the latest information from the staff on monetary developments had shown that Sudan's economic problems had reached crisis proportions. Although those problems had obviously been aggravated by adverse exogenous factors beyond the authorities' control, inadequate economic policies--especially under former administrations--might be the main reason for Sudan's economic plight. The authorities had recognized in principle the need for corrective action and had taken some measures, but it was evident that the steps taken thus far were insufficient to deal with the magnitude of the problem. A more decisive and comprehensive policy was clearly called for and should include short-term adjustment measures to address the most pressing imbalances in the fiscal and external accounts as well as medium-term structural reforms.

It was disappointing that the authorities, while agreeing in principle on the need for action, were delaying comprehensive measures, Mr. Grosche noted. In a number of critical areas, important differences of views between the staff and the authorities persisted, and there were no hints that those differences might soon be overcome. Thus, a further aggravation of the critical economic situation had to be expected, which would make it even more difficult and painful to redress the situation later. As experience in Sudan and other cases had clearly shown, the burden of adjustment grew when necessary measures were postponed. Moreover, the needed support from the international community would depend critically on the pursuit of the appropriate economic and fiscal policies; he thus urged the authorities to adopt the necessary comprehensive measures without any further delay and to settle their overdue obligations to the Fund. It was regrettable that the authorities had undertaken no further efforts to reduce their arrears to the Fund since the end of January 1986; in fact, Sudan's arrears had risen further since then.

Sustained action to reduce those arrears would also encourage the international community to support Sudan's adjustment efforts, Mr. Grosche suggested. It had been disappointing for the donors that had responded to the October 1985 reform package with additional bilateral aid to note that the package had failed. The authorities should be aware that they risked losing goodwill and that, in the future, more prior action might be needed to convince donors that their contributions would not be used to continue financial policies that were unsustainable in the medium term.

It was up to Sudan to take the first steps, Mr. Grosche concluded. Unfortunately, the authorities did not seem to understand that the situation had changed since the early 1980s when the international community--including the Fund--had stood ready to help Sudan without asking for much prior action, and that the message to be conveyed to them was quite different. In sum, only if Sudan first helped those who had assisted it already would it receive the additional help it needed. Finally, he supported the proposed decision.

Mr. Wijnholds said that it was sad that the Fund had had to declare Sudan ineligible to use its resources on February 3, 1986, but clearly it had had no other choice. Of course, such a declaration did not mean that there could be no further meaningful relations with the Fund, as was demonstrated by the current discussion of the 1985 Article IV consultation with Sudan. The staff should keep in contact with the authorities and assist them whenever possible to formulate a comprehensive adjustment program, the need for which had been recognized by the authorities.

It was clear from Sudan's very large external debt and the rather bleak medium-term outlook, with financing gaps of well over $1 billion per year over the next few years, that Sudan would need large and generous external assistance, Mr. Wijnholds considered. It was equally clear that for such assistance to materialize, Sudan would have to put appropriate measures in place. Some recent measures had gone in the right direction, and he hoped that more would be accomplished after the elections in April 1986.

Ms. Bush said that after many Executive Board discussions on Sudan over the past year, it was disappointing to review Sudan's general economic situation once again without having in view any clear prospects for a resolution of the problems. Particularly discouraging was the apparent lack of coordination of policies in the real and financial sectors in Sudan, so that what appeared to indicate progress in one area revealed problems in another. For instance, producer prices had been raised for farmers and a large increase in cotton production had occurred, helped by a return of favorable weather conditions. The authorities' attention to producer incentives was welcome. However, with the official exchange rate remaining overvalued, the Cotton Marketing Board could not earn enough revenues on export sales to cover the higher producer prices, and was thus incurring large losses that were being financed by extensions of credit from the central bank. Those losses could not be sustained in the long run, and it would be most unfortunate if farmers were unable to sell their output because a government entity could not afford to buy it. Such an outcome could do long-lasting damage to producer incentives by negating the beneficial effects of the recent producer price increases.

Furthermore, there was considerable room for decontrol of economic activity in Sudan, Ms. Bush suggested. Unfortunately, the authorities had increased the scope of administrative controls in an effort to allocate scarce resources while attempting to protect the lower-income groups from the price effects of full decontrol. The expansion of controls served mainly to drive economic activity into the underground economy, where it was quite likely that prices were much higher than they would otherwise be. For instance, the black market exchange rate was almost twice as high as the official rate, the rate at which exports and imports of basic goods were priced. If the exchange markets were unified at a rate that was free to move, the rate probably would settle below the current black market rate, given the high risk premium that must be attached to that illegal rate. In turn, consumer prices might fall and goods might become increasingly available as the black market faded in importance.

A welcome depreciation in the commercial bank exchange rate had narrowed the margin between it and the black market rate to 10-12 percent, Ms. Bush continued. That adjustment followed a period during which virtually no foreign currency remittances had been surrendered to the commercial banks, indicating a growing awareness on the part of the authorities that the exchange rate did influence market transactions. She hoped that supporting changes in the official rate would also soon be forthcoming. The ultimate exchange market unification, coupled with price control, would help to stimulate a broader domestic supply response, supporting the authorities' efforts to promote stronger growth.

Such general price and marketing decontrol--including an enhanced role for the private sector in production, distribution, and marketing--was the most meaningful supply-side measure that the authorities should undertake, Ms. Bush emphasized. Of course, supporting measures to contain the public sector's absorption of scarce resources would also be helpful.

The authorities should contain expenditures, and implement appropriate revenue measures designed to enhance incentives for savings and investment, because if private sector confidence was restored, investment could recover. Out of a rationalized, consolidated public sector--including the public entities--a restrained monetary policy could evolve, laying the ground for a more stable financial environment that could support real economic growth. Such a monetary policy should incorporate adequate real returns on financial savings as well, strengthening the incentives for Sudanese abroad to repatriate their earnings.

There was no doubt that generous levels of external assistance, preferably on concessional terms, would be required over the medium term to restore and support an adequate rate of growth, Ms. Bush commented. However, such external assistance could only be put to good use in the context of a comprehensive economic adjustment program that addressed the serious domestic imbalances and inefficiencies that characterized the Sudanese economy. Without prompt implementation of a broad spectrum of policies, such as those recommended by the Fund and Bank staff, it was difficult to envision that external donors would be prepared to provide the several billion dollars of debt relief and financial aid needed over the next few years to restore Sudan's imports to the levels required for domestic recovery, and improve its debt servicing capability over the medium term.

Unless the authorities adopted a broad-based economic strategy, few prospects remained for clearance of Sudan's ever-growing arrears to the Fund, Ms. Bush indicated. Her authorities were committed to assist Sudan in that matter, as had been indicated on numerous occasions over the past year, but the Sudanese authorities needed to address their economic problems fully before her authorities could carry out their commitment. Of course, Sudan would also need the assistance of other donors to make the economic adjustment effort viable. While donors would probably continue to provide a minimum of commodity assistance to help reverse some of the effects of the earlier drought, it was difficult to see how enhanced levels of aid--the kind that would provide the needed budgetary support as well--could be forthcoming in the absence of the comprehensive budgetary, monetary, exchange rate, and structural policies that were needed to create the environment in which such assistance could be utilized productively. If the Sudanese were to attain the "normative" medium-term outlook that included an average growth of 4 percent, such wide-ranging reform was necessary.

The authorities should be aware that their lack of concrete progress on economic reform and their lack of progress in clearing their arrears to the Fund were causing grave difficulties for all other members of the Fund, Ms. Bush stated. The Fund's income position had been eroded because overdue charges were being accounted for on a nonaccrual basis, and that had led to an increase in charges on Fund borrowing for all members, even those that were current on their obligations. Furthermore, the Fund might have to consider provisioning against overdue repurchases, which could raise charges even further, as a reflection of a further weakening of the Fund's financial position. She thus urged the authorities to consider the broader implications of their actions. As Mr. Foot and other Executive Directors had pointed out, ineligibility was not the end of the road, and the authorities should continue to work closely with the staff. Nevertheless, it was the responsibility of the authorities to act decisively to take advantage of the assistance that was being offered by the Fund and bilateral donors. Finally, she could support the proposed decision.

The staff representative from the Middle Eastern Department confirmed that most of the procurement prices that the authorities had introduced in the agricultural sector had either been recommended by the Bank and the Fund staff or had been endorsed by them. However, as some Executive Directors had pointed out, those prices had been based on certain expectations about the level of the exchange rate; since that level had not materialized, the established prices had contributed to a transfer of income to tenants financed by bank credit.

The Fund and Bank staff had recommended that the authorities increase land and water charges in the irrigated schemes by 60 percent, the staff representative continued. Although there had been a recovery of agricultural output, and higher prices had been proposed for the procurement of cotton, the authorities had indicated that a 60 percent increase in one year would be politically too difficult to negotiate with the tenants' unions. Subsequently, the new Minister of Finance had indicated that because agreement had already been reached on a 30 percent increase in the land and water charges, new negotiations were not possible; however, the Minister had added that, if conditions were favorable in the coming year, the authorities would attempt to increase the land and water charges to a level that would ensure a significant movement toward full cost recovery.

The staff had understood that the authorities intended to bring about institutional stability in the banking system, and that that would probably involve the implementation of a parallel system of banking--Islamic and non-Islamic--the staff representative added. However, the staff had no further information to indicate that the authorities had indeed introduced, legislatively or administratively, any changes in the banking system.

As Mr. Finaish had mentioned, the staff report had not provided detailed breakdowns by source for the aid flows to Sudan, the staff representative from the Middle Eastern Department recalled. However, in the section that discussed commodity and cash inflows, the main sources had been listed. Moreover, for 1985, the staff estimated that of the total cash and commodity aid of some $500 million that had been disbursed, a substantial contribution of about $205 million had come from Arab countries.

Mr. Mtei said that several important factors had considerably affected the outcome on the fiscal deficit and monetary expansion in Sudan. Although some institutional changes might have affected the expected government receipts, the significant slowdown in economic activity over the past three years had had an important bearing on tax and nontax revenues. In view of the large share of import duties in government revenues, the continued compression of imports had also adversely affected revenue performance. Three major factors had forced rapid expenditure expansion. First, the need to respond to the daunting economic challenge facing the country in 1984/85 as a result of the large-scale famine had led to considerable pressure on government expenditure. Although the generous response of the international community had helped considerably, the Sudanese Government had had to allocate sizable resources to help contain human suffering and prevent loss of life. Second, the influx of refugees across the eastern, western, and southern borders of the country--a total of 2 million people, according to the authorities' most recent estimate--had added to the pressure and had forced the Government to supplement the assistance provided by the international community to provide basic needs for the refugees. Finally, the continuation of civil disturbances and security problems in the south, with the resultant increased defense and security expenditures, had also contributed to the pressure on government expenditures. All of those developments--on the revenue and the expenditure sides--had been reflected in the expansion of bank credit to the Government and thereby of the money supply. With the return of normal weather, and increased hopes for an early settlement of the security problem in the south, the authorities were optimistic that they would be able to contain expenditure overruns and monetary expansion during the next year.

The authorities understood the critical nature of their external debt situation, and hoped that their current and intended policy measures would restore donors' and creditors' confidence, so that generous rescheduling and higher aid flows would follow, Mr. Mtei continued. The commensurate support of the international community in the form of extraordinary debt relief and aid was most essential for the success of the authorities' adjustment effort. As had been stressed by Executive Directors, assistance of the international financial community had to be an integral part of any cure prescribed for Sudan's grave situation.

The authorities intended to continue along the lines agreed with the staff on producer prices and on the liberalization of price and profit controls, Mr. Mtei stated. They were also working, with the assistance of the World Bank, to rehabilitate the major irrigation schemes in the agricultural sector and the key industries, including textile and sugar industries and the manufacturing sector. Substantial financial assistance for those projects was also coming from the Arab Fund. The authorities were also continuing their efforts to reform the parastatal sector so as to ensure the financial viability of the public enterprises.

The current Sudanese Government was in a state of transition, and while it had been stressing economic recovery and economic reforms over the past few months, its current preoccupation was the preparation and organization of elections so that a properly elected democratic regime could assume its responsibilities by end-April 1986, Mr. Mtei indicated.

It was hoped that the installation of the civilian government would provide added impetus to solve the economic and financial problems that were facing the country.

The Chairman then made the following summing up:

Executive Directors expressed broad agreement with the thrust of the appraisal in the staff report for the 1985 Article IV consultation with Sudan. They noted with great concern the very severe financial and economic imbalances facing Sudan. Recognizing that the imbalances had been aggravated by adverse external factors such as the effects of three years of drought, the inflow of refugees, and disruptions in the availability of foreign aid, Directors nonetheless stressed the role that had been played by the authorities' inadequate recognition of the gravity of the situation and by their delayed and insufficiently comprehensive policy actions.

While indicating awareness of the difficulties facing the authorities, Directors expressed concern and disappointment about further delays in taking corrective action, which would only make the task heavier and more painful. They emphasized that a strong, sustained, and comprehensive adjustment effort, formulated in a medium-term framework of economic recovery along the lines suggested by the Fund staff and supported by significant external assistance, would help restore financial stability and promote economic growth, which were essential for attaining balance of payments viability.

Directors emphasized that a viable adjustment effort should encompass supply-side and demand-management policies. They were pleased to note the alleviation of the drought conditions and commended the recent measures taken by the authorities to encourage agricultural production, including the adjustment of producer prices for cotton and other crops, but they stressed their concern that, as a result of inadequate exchange rate policies, the cotton marketing agency was facing unsustainable losses.

Directors observed that supply-expanding policies should be reinforced by effective demand-management policies. In that regard, they regretted the rapid rate of monetary expansion that had taken place in Sudan in the past two years, reflecting mainly the weak budgetary situation. While welcoming the adoption by the authorities of a number of revenue and expenditure measures, Directors, noting that budget revenue covered barely one half of outlays, stressed that much stronger action was needed to reduce the fiscal deficit and limit government borrowing from the banking system. It was observed that over the medium term, the authorities could improve the budgetary situation only by adopting fundamental fiscal reforms to contain expenditure, expand the revenue base, and improve tax elasticity. The resource mobilization effort should include, in particular, measures to improve the financial position of public enterprises.

Directors also underlined the importance of measures to promote private savings and investment. They recommended an early and effective implementation of price decontrol measures to provide a much-needed improvement in the environment for increased private sector investment activity.

Directors noted Sudan's precarious balance of payments situation, as reflected in an inability to meet external debt obligations and a compression of imports, which was having adverse effects on domestic production. Directors were generally of the view that an essential element of the comprehensive adjustment package should be a realistic and flexible exchange rate policy. In that connection, Directors noted the recent adjustment of the commercial bank exchange rate as a first step toward more realistic levels, but stressed the need for bolder action that could lead to an early unification of the exchange rates at realistic levels. Most speakers also pointed to the critical need for substantial external financial assistance in the form of additional aid and debt relief in support of Sudan's adjustment policies; indeed, it was felt that without such assistance the objective of promoting financial stability and economic growth on a sustained basis could not realistically be achieved. At the same time, it was also emphasized that without the implementation of a meaningful and comprehensive set of policies by Sudan, the resumption of external assistance on a high scale was not likely.

Directors expressed concern about Sudan's large overdue obligations to the Fund and stressed the urgency to begin implementation of a program involving both Sudan and the international community that would permit prompt and full settlement of those arrears. Notwithstanding the declaration of February 3, 1986, which made Sudan ineligible to use the Fund's general resources, Directors stated that the staff should continue to provide technical assistance to the authorities in the formulation of policies to address the serious economic problems facing Sudan. Directors welcomed Mr. Mtei's assurance that the authorities remained committed to discharge the arrears as early as possible and were willing to continue their cooperation with the Fund in quickly finding a mutually acceptable solution to Sudan's problems.

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

The Executive Directors then took the following decision:

1. The Fund takes this decision relating to Sudan's exchange measures subject to Article VIII, Sections 2 and 3, and in concluding the 1985 Article XIV consultation with Sudan, in the light of the 1985 Article IV consultation with Sudan con ducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. Sudan's exchange system includes multiple currency practices and restrictions on payments and transfers for current international transactions as described in SM/86/33. These restrictions are subject to approval by the Fund under Article VIII, Sections 2 and 3. The Fund urges the authorities to eliminate the restrictions on payments and transfers for current international transactions and to take appropriate steps toward an early unification of the exchange system.

Decision No. 8223-(86/45), adopted
March 12, 1986

4. SIERRA LEONE - OVERDUE FINANCIAL OBLIGATIONS - REVIEW OF DECISION ON COMPLAINTS UNDER RULE K-1 AND RULE S-1 AND NOTICE OF FAILURE TO SETTLE TRUST FUND OBLIGATIONS

The Executive Directors considered a staff paper on the further review of Decision No. 8014-(85/101) G/TR with respect to Sierra Leone's overdue obligations to the General Department and notice of Sierra Leone's failure to settle Trust Fund obligations, and the review of Decision No. 8173-(86/3) S with respect to Sierra Leone's overdue obligation in the SDR Department (EBS/86/47, 2/28/86).

The staff representative from the Treasurer's Department informed Executive Directors that a payment of $3 million had been received the previous day from Sierra Leone. That amount would be used to clear Sierra Leone's overdue obligations in the SDR Department, thus permitting the complaint under Rule S-1 to be withdrawn. Sierra Leone's payment had reduced its total overdue obligations to the Fund to SDR 14.6 million.

Mr. Mtei recalled that at the Executive Board's previous discussion of Sierra Leone's overdue obligations (EBM/86/3, 1/6/86), he had reported that the authorities had expected to make a payment of $3 million toward the elimination of the arrears. The authorities deeply regretted that, despite earlier encouraging signals, it had proved impossible to solicit a favorable response from their creditors to provide the necessary bridging loan. However, arrangements had finally been made so that $3 million could be transmitted to the Fund in partial settlement of Sierra Leone's obligations.

Although economic and financial conditions in Sierra Leone had continued to deteriorate, there had been two closely related encouraging developments, Mr. Mtei commented. First, the authorities had come to fully appreciate the nature and extent of their economic problem, and second, they had adopted the far-reaching measures required to arrest further deterioration and create the basis for sustainable growth. They hoped in particular that the measures would facilitate the channeling of export receipts into the banking system, which, in turn, would enhance Sierra Leone's ability to discharge its external obligations, including those to the Fund, in an orderly manner. The authorities were also hopeful that their adjustment program would promote external confidence and attract financial support from donors. In that context, the Fund's role was considered essential to help the authorities mobilize external resources, thereby enabling them to discuss the possibility of a stand-by arrangement.

The authorities were presently actively promoting a political atmosphere that would safeguard national security prior to the full implementation of the adjustment measures, which included a market-determined exchange rate system and price liberalization, Mr. Mtei mentioned. To that end, consultations were already under way with political pressure groups such as the labor congress, the teachers' union, the Chamber of Commerce, the employers' federation, as well as colleges, with a view to mobilizing support for the adjustment program. In those circumstances, it would be useful if the Executive Board were to adopt a decision that sent an appropriate signal to Sierra Leone to encourage the authorities to press ahead with their efforts. If a decision was taken to declare Sierra Leone ineligible, even to become effective at a future date, the authorities were likely to feel helpless and abandoned. He therefore urged Directors to review the situation further after two months had elapsed. In that way, the authorities and staff could make further progress on the ongoing consultations on the adjustment measures. The new Administration's willingness to implement measures that had hitherto been considered politically unacceptable was an encouraging sign, and it would be wise to take advantage of the current momentum for adjustment. The least that the Board could do in such circumstances was to adopt the first version of the fourth paragraph of the proposed decision.

The Chairman noted that the first version of paragraph 4 of the proposed decision stated that the Fund would review further its decision adopted June 28, 1985 limiting Sierra Leone's use of the Fund's resources, not later than May 5, 1986, and that a decision to declare Sierra Leone ineligible to use the Fund's general resources would be taken with effect on the date of the review, in the absence of full settlement of its overdue financial obligations. The second version of paragraph 4 of the draft decision stated that unless by May 5, 1986 Sierra Leone was current in its financial obligations to the Fund in the General Resources Account, it would become ineligible with effect on that date to use the general resources of the Fund. An indication from Executive Directors as to their preferred alternative would be helpful.

Mr. Wijnholds remarked that not much progress appeared to have been made since the complaint had been lodged regarding Sierra Leone's overdue financial obligations to the Fund, but the announcement of a payment of $3 million was a welcome development. The authorities were contemplating a comprehensive liberalization of the economy, and a Fund staff team was presently in Sierra Leone to review the situation. Given those developments, he was prepared to opt for the first version of paragraph 4 in the proposed decision.

Mr. Foot, stating his regret that another review had been necessary, recalled that Sierra Leone's arrears had arisen at the same time as those of Liberia, which had been declared ineligible some time ago. The differences between the two countries were that Sierra Leone had made a payment of $3 million, and that the authorities were considering a comprehensive adjustment program, although until political support could be obtained internally, that program could not be translated into action.

It was far from clear to him that the recent change of government explained the delays in the adjustment efforts, or that the measures currently proposed were enough, although he had been encouraged by the staff's comment in EBS/86/47 (2/28/86) that the new program appeared to be going in the right direction, Mr. Foot indicated. What was especially important was that action be taken promptly and that it be far-reaching particularly with respect to the increases in producer prices and the implementation of the floating exchange rate. In a number of member countries, the authorities apparently had avoided full unification of the exchange rate in order to limit the perceived adverse effects. He wondered what sort of mechanisms would be available to implement the proposed new regime, and whether the Fund could provide technical assistance in that connection. It was not clear whether the official rate was intended to be separate from the interbank rate, or how many banks might set the latter rate; therefore, the prospects under current circumstances for a genuinely free market rate were uncertain.

Having said that, he wished to point out that the Fund should not turn its back on any serious chance of returning to normal relations with Sierra Leone, Mr. Foot added. Although he preferred the second version of paragraph 4--ineligibility after a given time had elapsed--he gave weight to what Mr. Mtei had said about the signal that that would give. If there was a consensus among Executive Directors in favor of the first version of paragraph 4 in the proposed decision, he would be prepared to go along, on the clear understanding that that time would have run its course by May 5, 1986 if major progress had not been made.

Mr. Grosche said that he had hoped that the staff would announce a positive outcome of its recent discussions with the authorities on a comprehensive adjustment package. However, in view of Sierra Leone's recent payment, Mr. Mtei's statement that the authorities were clearly resolved to adopt a comprehensive adjustment package, and the measures that the authorities had already taken, he could go along with the first version of paragraph 4.

Mr. Leonard said that he agreed with other speakers that there had been signs of movement in Sierra Leone and that there were some grounds for hope that the economic situation could be rectified. Thus, he was prepared to support the first version of paragraph 4 in the proposed decision. However, he wished to suggest an amendment to paragraph 3 of the proposed decision, which referred to the measures recently announced in the exchange rate and pricing policy areas, but not to the liberalization of import licensing, a measure of no less value than the other measures that had been taken. He thus proposed that the paragraph be reworded to state, "the Fund notes the measures recently announced by Sierra Leone in the exchange rate, pricing, and import licensing policy areas...."

Mr. Suraisry said that he had planned to support the second version of paragraph 4 in the draft decision. However, in view of the amount that had recently been paid by the authorities, and in the light of the measures that they had taken and would be taking, he could go along with the first version, providing for an additional review. Nevertheless, it was important to remember that even after the recent payment of $3 million, Sierra Leone's arrears to the Fund were currently more than they had been at the second review. The forthcoming review would be the fourth one, and time was running out.

Mr. Ercel said that, taking into account the measures that had been recently adopted by the authorities and their intention to continue the comprehensive adjustment effort, he could go along with the first version of paragraph 4 of the draft decision.

Ms. Lundsager said that she was pleased that the authorities had made a payment, but she was somewhat disappointed that it had been received after a lapse of two months. She was confused about the exact status of the comprehensive adjustment program because it had been discussed over a number of months. In the summer of 1985 a technical assistance team from the Fund had been providing advice to Sierra Leone on how to work toward unification of the exchange system, which had not yet been implemented. It appeared that a staff team was once again in Sierra Leone. At the previous meeting on Sierra Leone (EBM/86/3, 1/6/86), Mr. Mtei had been hoping full implementation would have occurred, and that the rest of the package would have fallen into place without bridging assistance, so that there would not be a need for another discussion.

Even though she had some reservations about the full commitment of the authorities to the comprehensive adjustment measures, she was willing to give them the benefit of the doubt, and was prepared to go along with the first version of paragraph 4, Ms. Lundsager concluded. However, if after two months the authorities had not made further concrete progress in implementing those measures so that a full package could be put together to clear the arrears, her authorities would be inclined to declare Sierra Leone ineligible to use the Fund's resources.

Mr. Orleans-Lindsay said that Sierra Leone's partial settlement of its overdue financial obligations to the Fund was a belated but significant step in its efforts to resolve its problems. He was encouraged that the authorities had adopted important measures, the sustained implementation of which would help to prevent a further deterioration in the country's economic and financial situation and would enhance its capacity to fulfill its external financial obligations, including those to the Fund. In the light of those developments, he would opt for the first alternative of paragraph 4 of the proposed decision, to allow the new Administration more time to organize and put the additional adjustment measures in place.

Mr. de Forges said that despite the authorities' pledge to do their utmost to settle their arrears, and even though a belated payment had been made, the arrears that had amounted to SDR 13 million at the end of 1985 currently totaled SDR 14 million. Those arrears could reach SDR 22 million within three months and more than SDR 35 million by the end of 1986. In the light of those developments, and given that the current review was the third one, a clear signal should be given to the authorities. Initially, he had been inclined to support the second version of paragraph 4 of the proposed decision. Nevertheless, taking into account the presence of a staff mission in Sierra Leone and the measures recently announced, he could very reluctantly go along with the first version of the paragraph.

Mr. Isleifsson said that he welcomed the recent economic measures adopted by the Sierra Leone authorities as well as the $3 million payment to the Fund. Based on those developments and the comparison of Sierra Leone's situation with that of other members and a similar stage that was provided in Attachment IV of EBS/86/47, he could go along with the first version of paragraph 4 of the proposed decision.

Mr. Zecchini stated that he welcomed the payment that Sierra Leone had made. He was also pleased to see that the authorities were showing a greater measure of willingness to adopt an adjustment program. Given those new elements, and the need to apply a treatment that was easily comparable with previous similar situations, he was inclined to support the first version of paragraph 4 in the proposed decision. He also wanted to support that option because the specific provision that the decision to declare Sierra Leone ineligible would be taken with effect on the date of the review--namely, May 5, 1986--made it very similar to the second option.

The staff representative from the African Department said that the staff had been discussing a floating exchange rate system with the Sierra Leonean authorities since February 1985, in connection with the first technical assistance mission. However, the authorities had decided to devalue the leone and discussions on the floating exchange system had not progressed until early in 1986. After another Fund mission had visited Sierra Leone in February 1986, the authorities had prepared a package of measures, including the exchange system reform, producer price increases, retail price increases, and other liberalization measures, which had been approved subsequently by the President and a special Cabinet session. The authorities had then requested technical assistance from the Fund for the implementation of the floating exchange regime, and a staff member had been sent to Freetown on February 20. At the same time, the President had convened a widely publicized meeting with representatives of the labor congress, teachers' union, and Chamber of Commerce to inform them about the measures that would be implemented. Because the President was to leave the country the following day, the authorities had hesitated to implement such a far-reaching, sensitive package of measures until his return on March 11. The staff hoped that the measures would be implemented, even though so much time had elapsed since the Cabinet had approved the package of measures; however, it was not taking the situation for granted, and was keeping in close touch with the authorities.

The authorities had requested that an expert be recruited to help them implement the floating exchange regime, the staff representative from the African Department concluded. However, the situation in Sierra Leone was not comparable to that of other members, as suggested by Mr. Foot, because a Fund resident representative was already in the field. Moreover, because the new system had been discussed for over a year, many of the commercial banks, as well as the Bank of Sierra Leone, were fully cognizant of what needed to be done in the context of the new exchange system.

The staff representative from the Treasurer's Department suggested the addition of a new first sentence to paragraph 2 of the proposed decision, reading "the Fund welcomes the recent payment by Sierra Leone." The remainder of the paragraph would remain as originally written. Moreover, in the first version of paragraph 4, the reference to Decision No. 8173-(86/3) S relating to overdue obligations in the SDR Department should be deleted, to reflect the recent payment by Sierra Leone.

The Executive Directors then adopted the following decision:

1. The Fund has reviewed further Decision No. 8014-(85/101) G/TR, adopted June 28, 1985, and Decision No. 8173-(86/3) S, adopted January 6, 1986, in light of the facts described in EBS/86/47 (2/28/86), pertaining to Sierra Leone's overdue financial obligations to the Fund.

2. The Fund welcomes the recent payment by Sierra Leone. However, the Fund regrets the continuing nonobservance by Sierra Leone of its financial obligations to the Fund and notes that further substantial obligations will fall due in the near future. The Fund again urges the Sierra Leonean authorities to make full and prompt settlement of the overdue financial obligations to the Fund.

3. The Fund notes the measures recently announced by Sierra Leone in the exchange rate, pricing, and import licensing policy areas and again calls upon Sierra Leone to adopt a strong and comprehensive program that would result in necessary economic adjustment.

4. The Fund shall review further Decision No. 8014-(85/101) G/TR not later than May 5, 1986, taking into account any further developments. It is expected that a decision to declare Sierra Leone ineligible to use the Fund's general resources, pursuant to Article XXVI, Section 2(a), will be taken with effect on the date of the review, in the absence of full settlement of Sierra Leone's overdue financial obligations to the Fund in the General Resources Account by that date.

Decision No. 8224-(86/45), adopted
March 12, 1986

APPROVED: November 18, 1986

LEO VAN HOUTVEN
Secretary