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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 86/158

3:00 p.m., September 17, 1986

J. de Larosière, Chairman

Executive Directors	Alternate Executive Directors
A. Alfidja	Mawakani Samba
	J. K. Orleans-Lindsay, Temporary
C. H. Dallara	D. C. Templeman, Temporary
	E. L. Walker, Temporary
	G. Seyler, Temporary
	M. Z. M. Qureshi, Temporary
	M. Sugita
	W.-R. Bengs, Temporary
	Jiang H.
	S. Ganjarerndee, Temporary
A. Kafka	
	M. Foot
	O. Isleifsson, Temporary
	L. Leonard
	O. S.-M. Bethel, Temporary
	A. Abdallah
	J. Abramovich
	L. K. Ebrill, Temporary
	J. de la Herrân, Temporary
	V. Rousset, Temporary
J. J. Polak	
	A. V. Romuâldez
G. Salehkhou	
A. K. Sengupta	A. Vasudevan, Temporary
	N. Kyriazidis

L. Van Houtven, Secretary
B. J. Owen, Assistant

Also Present

IBRD: P. M. Landell-Mills, Western Africa Regional Office; P. Watson, Eastern and Southern Africa Regional Office. African Department: A. D. Ouattara, Director; J. Artus, D. T. S. Ballali, E. A. Calamitsis, C. V. Callender, D. J. Donovan, K. G. Dublin, U. R. Gunjal. Exchange and Trade Relations Department: E. H. Brau, S. Kanesa-Thasan, L. Hansen. External Relations Department: C. S. Gardner, Deputy Director; J. M. Landell-Mills. Fiscal Affairs Department: V. Tanzi, Director; M. I. Blejer, C. Schiller. IMF Institute: Y. Pamire, Participant. Legal Department: J. G. Evans, Jr., Deputy General Counsel; H. Elizalde, J. M. Ogoola. Middle Eastern Department: E. B. Maciejewski. Research Department: M. P. Dooley, D. Folkerts-Landau, P. Isard, N. M. Kaibni, M. D. Knight, A. Lanyi, P. R. Menon, R. Pownall. Secretary's Department: J. W. Lang, Jr., Deputy Secretary; G. Djeddaoui. Treasurer's Department: D. V. Pritchett. Personal Assistant to the Managing Director: R. M. G. Brown. Advisor to Executive Director: M. A. Weitz. Assistants to Executive Directors: J. R. N. Almeida, F. Di Mauro, R. Fox, S. King, T. Morita, J. A. K. Munthali, A. H. Mustafa, W. K. Parmena, B. Tamami, H. van der Burg, E. L. Walker.

1. THE GAMBIA - 1986 ARTICLE IV CONSULTATION; STAND-BY ARRANGEMENT; STRUCTURAL ADJUSTMENT ARRANGEMENT; AND USE OF FUND RESOURCES - COMPENSATORY FINANCING FACILITY

The Executive Directors resumed from the previous meeting their consideration of the staff report for the 1986 Article IV consultation with The Gambia, a request for a stand-by arrangement, and a request for an arrangement under the structural adjustment facility (EBS/86/189, 8/19/86), together with a staff paper on a request expected to be received from The Gambia for a purchase under the compensatory financing facility in an amount equivalent to SDR 4.71 million (EBS/86/193, 8/19/86). They also had before them a background paper on recent economic developments in The Gambia (SM/86/216, 8/27/86).

The staff representative from the African Department explained that in 1986/87, it should be possible for The Gambia to cover its remaining financial gap almost entirely through debt relief. Concessional loans and other assistance already obtained in the context of efforts under way since the donors' conference in 1985 had been taken into account in the program.

The sharp reduction in the rate of inflation expected in 1986/87--to 16 percent from 42 percent in the previous year--should be attainable, the staff representative continued. It should be borne in mind that the exchange rate had stabilized in recent weeks, whereas in 1985/86 it had depreciated by about 130 percent in local currency terms. Similarly, the price of rice, which had risen sharply in 1985/86, had since stabilized and in fact fallen. In addition, monetary policy was tighter.

The budget deficit was expected to rise sharply in 1986/87, for the reasons outlined in the staff report, but the authorities had indicated their intention to reduce it over the following two years by as much as 8 percent of GDP, the staff representative remarked. There were a number of ways in which they would pursue that objective. First, transfers to the groundnut sector were a major candidate for reduction, since they amounted at present to about 9 percent of GDP. In addition, and apart from generally tight control over expenditures and improved revenue collections, both the staff and the authorities felt that everything possible should be done to increase domestic taxes even though the increase in revenue from that source might not be large in absolute terms.

The net savings in 1986/87 from the envisaged reduction in civil service personnel were not expected to be large owing to the cost of paying gratuities, accumulated leave, and pensions, the staff representative noted. However, the authorities estimated a reduction in expenditure of about D 4 million on that account. The reductions in personnel planned for August 31, 1986 had been implemented and in fact had made a larger number of personnel redundant than had been mentioned in the targets set forth in the authorities' memorandum of economic policies. The full impact of the retrenchment in the civil service would not be felt until the following year.

As mentioned in the staff appraisal, additional fiscal adjustment might well prove to be necessary, particularly if groundnut prices did not rise, the staff representative added. At the same time, if the deficit was largely or entirely due to development expenditures that were financed by concessional funds, its impact on the balance of payments might not be too severe.

The groundnut sector, and groundnut pricing policy in particular, raised complex issues that should probably have been covered more thoroughly in the staff report, the staff representative commented. Cross-border trade in groundnuts was by no means a new phenomenon; but the size--and even, on occasion in the past, the direction--of such flows was difficult to estimate, given the open nature of The Gambia's border and its close commercial and other ties with neighboring countries.

In 1985/86, the producer price for groundnuts had been raised three times, the staff representative recalled. In July 1985, it had been raised to the neighboring country's price, calculated at the prevailing exchange rate on the parallel market, and in November, it had been raised to take account of a further depreciation of the dalasi. In early December, the dalasi had depreciated rapidly owing to speculation about the introduction of the new exchange system in January 1986, and the producer price had lagged behind the more appreciated parallel exchange rate. Domestic institutional difficulties were among the considerations leading the authorities to delay a further increase in the producer price, which was based on a number of different elements, including developments in the world price for groundnuts; it had also taken time to gather the necessary information. Despite their concern about the possible cost to the Gambia Produce Marketing Board (GPMB), or to the budget, the producer price had been increased to the cross-border price in mid-January 1986. In the intervening weeks, there had been some cross-border outflows of groundnuts, although at the beginning of the season, the authorities believed that there had been inflows as a result of certain problems associated with the extension of credit across the border, whereas in The Gambia, farmers were paid in cash.

The problems faced by the Gambian authorities had become much more acute with the further fall in world groundnut prices, which had declined by 50 percent between May 1985 and May 1986, when the authorities had decided once more to increase the producer price to the cross-border level, involving substantial losses, the staff representative stated. The authorities had indicated that that pricing policy was temporary and that action would be taken to ensure that such losses were essentially eliminated by 1988/89. An increase in world prices, or a change in the producer pricing policy of a neighboring country, would make a social contribution in that respect. Another solution that had been discussed with the authorities was the one suggested by Mr. Polak, namely, that the authorities should refrain from competitive pricing, accepting the fact that a large part of the groundnut crop would go across the border, and that the exports of the GPMB would decline, leading to a shortfall in its earnings. While there was no reason why the Central Bank should not seek to buy back the equivalent amount of foreign exchange from the farmers or the banking system to make up for that shortfall, both the authorities and the staff tended to agree that there were drawbacks to implementing such a policy immediately. It would be recalled that efforts to close the financing gap had not come fully to fruition at the time, and a large part of the Central Bank's foreign exchange inflows, which were included in the financing package, had consisted of the earnings of the GPMB. To replace relatively assured inflows of about SDR 10 million with a plan for the Central Bank to buy back SDR 10 million from the market at some future date seemed to cast doubts on the credibility of the overall financing plan, particularly given the creditworthiness of The Gambia and the reluctance of some creditors involved in the financing package to provide new funds in the absence of assured sources of foreign exchange inflows. The authorities had also been mindful of the major one-way intervention in the exchange market by the Central Bank that would have been involved, at a time when the new exchange system had begun to work well but was by no means firmly established. Moreover, the Central Bank had not been intervening in the exchange market, and a policy that relied on intervention might have had an adverse psychological impact on market participants. In addition, there were certain institutional problems, including the possibility that foreign exchange earnings might not be expatriated, given the existence of a type of barter trade. Taking all those factors into account, there had been an agreement between the staff and the authorities that although the approach favored by Mr. Polak might be the most appropriate one to follow in the future, especially since the exchange system was working much better, it was necessary to maintain the existing policy for the time being.

The staff representative from the Exchange and Trade Relations Department observed that The Gambia's Fund position during the period of the proposed stand-by arrangement--including its use of the compensatory financing facility--was outlined in Table 1 of EBS/86/189. If the table had included a column for June 30, 1986, the member's total outstanding use of Fund credit, including overdue obligations, would have been shown as equivalent to 129 percent of quota at that time, 10 percent of which represented overdue charges; the figure for June 30, 1984 would have been 170 percent of quota. As indicated in the table, The Gambia's outstanding use of Fund credit would continue to decline through 1987, relative to 1986, even including the immediate disbursement of an amount equivalent to 20 percent of quota under the structural adjustment facility.

It would be desirable, in principle, given The Gambia's precarious debt service position, to reduce further its access to relatively high-cost credit, the staff representative commented. However, given the adjustment effort that he understood had been judged broadly appropriate for the year ahead (reduced access to such credit would require the provision of increased official development assistance), and the authorities had had great difficulty in attracting such additional concessional assistance. The rationale for proposing that The Gambia be granted access to 30 percent of its quota under the stand-by arrangement was thus catalytic. The country had heavy debt service obligations and, would continue to rely for some years on exceptional financing from various sources; larger access to relatively expensive financing would only aggravate the problem. In sum, The Gambia's need was for increased official development assistance, in keeping with an appropriate adjustment stance.

Although the staff would prepare a fuller analysis of the member's ability to service its obligations to the Fund in future, the staff representative continued, an attempt had been made in Table 8 to indicate as clearly as possible the debt service outlook, including a breakdown of debt service payments to the Fund and to other creditors. A similar analysis was contained in Appendix IV, on page 79 of EBS/86/189, in which repurchases from the Fund over the period to 1990/91 were clearly set out, together with an indication of exceptional financing in the short term and the remaining financing requirement, which it was also hoped would be on concessional terms. The outlook with respect to The Gambia's financial obligations to the Fund was described on page 26 of EBS/86/189.

A judgment on the appropriateness of the staff analysis would have to be based on the design of the program and the authorities' commitment to implementing it, both of which would ensure The Gambia's capacity to repay the Fund, the staff representative considered. The two key factors were the flexible exchange rate policy that was being pursued, and a complementary flexible interest rate policy. Those policies would ensure, in contrast to the recent past, that the authorities would have access to foreign exchange for official debt service. In addition, as noted in the staff report, the need to build up reserves was a central feature of the program stressed by the authorities in their letter of intent. In fact, through December 1986, cash payments with respect to external arrears were being held flat. Priority was being given in the first instance to increasing gross reserves because the cost of not being able to meet fluctuations in debt service payments was extremely high. It should be noted as well that the authorities had stated in the letter of intent that they would be prepared to purchase foreign exchange on the exchange market for the purpose of raising gross reserves and discharging official debt service obligations.

The Gambia's relative success with a floating exchange rate arrangement, compared with experience in other countries, reinforced a conclusion that the staff had reached in a paper on recent experience with floating exchange rates in developing countries, the staff representative from the Exchange and Trade Relations Department recalled. Apparently, interbank arrangements like that of The Gambia worked better than auction arrangements, for the general reason that well-established commercial banks were competing with the parallel market and in essence replacing it. Auction arrangements were administered by the authorities, entailing a much higher probability of administrative interference, especially if an auction rate was not satisfactory, both with respect to sales of foreign exchange in the market and access to the market, thereby undermining the credibility of the auction arrangement. Erratic rates of foreign exchange sales in the auction market did not give participants enough confidence to surrender foreign exchange to the central monetary authorities.

The staff representative from the Research Department explained that under the Fund's policy on compensatory financing, the calculation of export shortfalls did not include re-exports. According to the UN classification, re-exports were defined as imports which were subsequently exported with no change in their physical characteristics. A reduction in re-exports in a given period was assumed to reflect a similar reduction in imports in an earlier period, so that the impact on the balance of payments was roughly neutral. Had the calculations been made on the basis of data including re-exports, the shortfall would probably be larger--because the export base would have been larger--than if the calculations had been estimated on the basis of domestic exports only. In fact, The Gambia's export base would be five times larger if re-exports were included, and any percentage change would cause larger absolute shortfalls than if the same percentage was applied to the smaller base.

The price projections included in the calculations implied only a slight decline of about 1 percent from the depressed prices in the shortfall year, the staff representative added. The recovery in earnings projected for the two years ahead was expected to result from a recovery in the volume of exports of about 20 percent per annum on average. For later years prices were expected to recover in nominal terms by about 7 percent annually through 1991. Considering the extent of the decline in prices--about 50 percent--over the past two years, and the expectation that prices would stagnate for two more years, the staff had assumed that high-cost producers would cut back output in time to bring about some recovery in prices for the period through 1991. However, even the prices projected for 1991 would be some 15 percent below the prices realized in the early 1980s. It should be noted that the price projections had been made by the staff in close collaboration with the staff of the World Bank. Every effort was being made to improve the projections and to increase the frequency of joint exercises with the World Bank.

Mr. Dallara remarked that he had noted the downward trend in The Gambia's exposure to the Fund, even including the envisaged use of resources. However, he had taken little comfort in that fact because experience had shown that The Gambia's earlier use of Fund resources had perhaps been allowed to reach inappropriate levels of exposure. Experience also showed that the package before the Board was due not only to the very strong efforts of the Gambians but also to exceptional efforts of donors and banks, thereby underscoring in some ways the fragility of the country's debt service position.

Although the program design should offer some assurance in an analysis The Gambia's capacity to repay, Mr. Dallara added, that assurance was more applicable in the case of the structural adjustment facility arrangement since there was every expectation that the authorities would continue their adjustment effort. However, the program design had little relevance to the proposed purchase under the compensatory financing facility, beyond setting the disbursement date for the drawings.

Finally, the absence of any provision for the reduction of external arrears during the initial period of the program was rather unusual, Mr. Dallara considered. The implication of the performance criteria, although it was not made specifically clear, was that at the first review of the program, a precise figure for arrears would be agreed to, presumably a lower figure than the current amount of external arrears. While he appreciated the comments that had been made by the staff about the exchange system and the authorities' capability to enter into the exchange market, he felt that, in reality, that was a limited capability and one that would not enable them to eliminate external arrears or meet future debt service obligations with any certainty, given the substantial arrears that would remain in the period ahead.

Mr. Leonard said that he recognized that the calculations in the staff paper on The Gambia's request for a purchase under the compensatory financing facility had been made as a matter of policy. His concern was the appropriateness of that policy, an issue that could not be resolved at the present meeting. However, the relationship between re-exports and imports was less a 1:1 relationship than a 2:1 relationship. A significant degree of value added to the imports in The Gambia meant that those re-exports made a substantial contribution to export earnings. In addition, there was an element of import content in almost all exports that might be even harder to define than the import content of re-exports. Therefore, he had been slightly unhappy that the impact on The Gambia's total export effort of re-exports, including the considerable value added, had had to be ignored in arriving at the appropriate amount of compensation for its export shortfall under the decision on the compensatory financing of export fluctuations.

Mr. Foot agreed with Mr. Leonard; the application of the existing policy could result in totally unrealistic calculations, particularly if an import to which value was added in the home country for re-export fell in price. Theoretically, an apparently large export shortfall could then be considered to have been the result of taking into account the reduction in exports without taking account of the associated decrease in the import price.

The staff representative from the Research Department recalled that the Executive Board had examined the issue raised by Mr. Foot and Mr. Leonard some years previously. As noted before, the staff had adopted the UN definition of re-exports, namely, goods exported that had previously been imported but whose physical characteristics had not been altered. It could be argued that any domestic export had an import content and that the import content should be excluded from the calculation. To take an extreme case, the country might import crude oil and export petroleum products. Again, the Executive Board had discussed the issue and had decided that the calculation of the export shortfall would be based on the gross value rather than on the value added. It was extremely difficult to separate the import content of exports, particularly in a manner that would ensure uniformity of treatment for members requesting purchases under the compensatory financing facility.

The staff representative from the African Department, in response to a question by the Chairman, explained that Table 8 showed debt service as a percentage of purely domestic exports as well as a percentage of domestic exports plus that share of re-exports estimated to be the markup or profit. Re-exports were three or four times the size of domestic exports, and the markup would produce quite a large difference in the ratio of debt service payments to exports of goods and services.

The figures on re-exports were very uncertain because re-exports were not recorded directly at all, the staff representative from the African Department added. The figures in Table 8 had been based on an indirect method, involving a survey of businessmen and inquiries about the percentage of the import content of re-exports, as well as about the average rate of markup and profit. In addition, the figures were subject to considerable change as well as being unreliable. No doubt one problem with respect to the calculation of re-exports in the case of The Gambia was that it would have to be based totally on estimates.

The staff representative from the Research Department, also in response to a remark by the Chairman, said that no attempt had been made when the issue had been discussed previously to separate the value added element, even though the physical characteristics of the product in transit had not been altered but some other service within the country had been rendered to the product. The subject could of course be reconsidered by the Executive Board in the context of the review of the compensatory financing facility.

Mr. Foot agreed that the Executive Board would need to return to the issue at some stage.

The staff representative from the Western Africa Regional Office of the World Bank said that the whole process of improving the management of the parastatal sector was in the hands of the National Investment Board. Consultants had been working with the Board to strengthen its performance and had also been working specifically on three of the most important parastatals--the GPMB, the Port Authority, and the Utilities Corporation--with which it was expected that performance contracts would be signed before the end of the year. Impressive progress had been achieved by the National Investment Board, which was also handling the divestiture program, a detailed plan being expected before the end of the year.

With respect to the tourism sector, long-term potential was very promising in the view of the consultants whose preliminary report would shortly be finalized and used as the basis for an action program to develop that sector, the staff representative continued. Nonetheless, the industry faced some fairly serious immediate problems, particularly in restructuring the financing of the hotels, and much would depend on the ability of The Gambia to attract overseas investors into that sector. The staff's impression was that the reforms that had been introduced and the improved macroeconomic performance were important in improving the environment and attracting new investors.

The Investment Code was under revision, the staff representative added, and a new, simplified code that it was hoped would be enacted before the end of the year should speed up the administrative process, increase its transparency, and reduce the extent of the bureaucratic discretion.

On the more difficult question of the economy's long-term growth potential, the staff of the World Bank estimated that a rate of growth of between 3 and 4 percent a year should be possible if the Government carried through the structural adjustment program as envisaged, the staff representative stated. The rate of growth in the past five years had been under 2 percent. A great deal would depend on the future of the groundnut industry, and although price prospects were not as bright as one would wish, output was very low at present compared with the long-term average--under 50,000 tons compared with 90,000 tons in the past. A modest increase in output could therefore be expected, on a secular trend, allowing for exhaustion of the soil and increased desertification. There was no evidence that The Gambia was a less efficient groundnut producer than, say, Senegal, although there was some evidence that the seed stock had been allowed to deteriorate in recent years. But an effort had been made to tackle that problem.

As for the diversification of the economy, other sectors had potential for growth, the staff representative commented. Tourism had been projected to grow at a rate of 4 percent in 1986, fisheries at 6 or 7 percent, and manufacturing at 4 percent. The projections were tentative, but those sectors had shown a good capacity to grow in the past, and the measures taken recently by the authorities should enable that identified potential to be exploited in future. Manufacturing output should grow by 4 percent, from what was currently a very low base. The World Bank staff was preparing a project--perhaps the most important one currently--to promote the growth of the industrial sector. And performance of the development bank, which had posed a serious problem in the past--hindering both development and short-term financial management--was also being tackled.

A major project in the agricultural sector would be a subject of a midterm review in the fall, the staff representative from the World Bank stated. The significant unused resources of that project would, it was hoped, be redirected to improve agricultural performance in light of experience of the past two or three years.

The preparation of a population health project was well advanced, the staff representative from the World Bank continued, the objective being to deal with the fundamental issue of long-term demographic growth and the impact on long-term development. The Gambian authorities had been very forward thinking in the discussion of the project and in facing up to their population problem. In conclusion, the World Bank expected to be involved in projects, in addition to the structural adjustment operation, using external financing, including cofinancing, of about $40 million.

Mr. Abdallah remarked that in view of the time that the Executive Board had devoted to The Gambia, a small country with a narrow resource base, he would state simply that the country was facing a serious situation and that, in the final analysis, the question was what the Fund and the World Bank could do to help. It seemed to some Directors that use of the Fund's resources under a given facility was not suitable; yet the country's need for financial assistance was demonstrable. Perhaps it was necessary to give the authorities an indication of possible alternative sources of financing. No doubt the use made by member countries of the compensatory financing facility could be reconsidered when that facility was reviewed by the Executive Board.

The Chairman made the following summing up:

> Executive Directors, noting the serious deterioration in The Gambia's economic and financial situation in recent years, welcomed the adoption by the authorities in mid-1985 of a comprehensive adjustment program. In 1985/86 several major policy actions had been implemented. Furthermore, the authorities had undertaken to strengthen their adjustment effort during 1986/87 and the medium term, in support of which The Gambia had requested the use of Fund resources under a stand-by arrangement, the structural adjustment facility, and the compensatory financing facility.
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> Directors considered the introduction of the flexible exchange rate system in early 1986 to be a bold and appropriate step which, after some initial difficulties, had achieved considerable success in a relatively short period of time. The depreciation of the exchange rate had led to a sharp reduction in the scope of the parallel exchange market and had increased significantly foreign exchange inflows to the banking system. The authorities' assurances that they intend to monitor closely the evolution of the system in the period ahead to ensure that the process of exchange rate determination was fully flexible was welcomed. The new system had been accompanied by the decontrol of the retail price of rice and by sharp upward adjustments in other administered prices. The importance of continuing to ensure a full and timely pass-through of exchange rate changes to those administered prices was stressed. The decision to maximize official foreign exchange earnings by adjusting the producer price of groundnuts in line with those prevailing in neighboring countries posed a difficult policy dilemma for the authorities, as it entailed a large budgetary transfer to the groundnut sector, given prevailing world market prices. However, noting the intended temporary nature of this transfer, Directors supported the authorities' intention to undertake during 1986/87 a review of producer pricing policy and existing official groundnut marketing arrangements. Indeed, the restoration and maintenance of the economic viability of the groundnut sector was a major challenge to the authorities, Directors observed.

Directors noted that significant progress was achieved during 1985/86 toward ensuring a tighter fiscal policy stance, but it was noted that The Gambia's government sector was large and did not promote maximum efficiency. While the reduction in the overall budgetary deficit (excluding grants) from 18 percent of GDP to 9.3 percent was due largely to an unplanned cutback in development expenditures, significant improvements had taken place in revenue performance and in controlling current expenditures. Although the budgetary deficit was planned to increase significantly in 1986/87, it was recognized that this mainly reflected an expected return of development expenditures to more normal levels and the temporary transfer to the groundnut sector, and it was noted that most of the increase in the budget deficit would be covered by grants. However, the importance of achieving the envisaged major reduction in the budget deficit over the medium term was stressed. In that connection, the need to eliminate the deficit of the Produce Marketing Board was underscored.

It was emphasized that, in view of the highly uncertain external outlook, additional fiscal adjustment beyond that presently called for would prove necessary. An important start had been made in 1985/86 in tackling excessive government employment, and the authorities were encouraged to proceed resolutely with the planned further reductions in the size of the established civil service. The Government's decision not to grant any increase in civil service salaries was welcomed. The need for divestiture and rationalization in the parastatal sector was also stressed. Directors welcomed the intention to reform the tax system in order to reduce reliance on taxes on international trade while increasing the use of domestic taxes, including the possibility of introducing a general sales tax in the 1987/88 budget.

Directors expressed concern that some slippages had taken place in the implementation of credit policy during 1985/86, and they stressed the crucial importance of ensuring full adherence to the credit ceilings set by the monetary authorities. The recent actions taken regarding interest rate policy, including the introduction of a tender system for treasury bills, were viewed as positive steps in support of the adjustment process.

Directors supported the close collaboration between the staffs of the Fund and the World Bank and the authorities in designing medium-term policies to address the structural problems of the productive sectors of the economy. In this context, achieving a significant recovery of groundnut production was of crucial importance, but the narrower resource base underscored a pressing need to promote growth and exports in other sectors such as tourism and fisheries. Directors also supported the authorities' intention to agree with the World Bank staff on a revised public investment program by end-1986.

Despite the adjustment measures being taken, Directors stressed that The Gambia's external position would continue to remain extremely tight, as evidenced by the heavy debt service burden and the overhang of external arrears, as well as by the substantial external financing requirement likely to be present during each of the next three years. The provision of significant external assistance in support of the authorities' efforts was welcomed. However, several Directors drew the conclusion that the authorities should aim to achieve a larger improvement in the fiscal and external accounts than presently envisaged for the next three years, and they urged the authorities to stand ready to implement additional adjustment measures. Moreover, for normal relations with creditors to be restored, it was considered crucial that the authorities take all necessary steps to ensure that The Gambia is current in its nonreschedulable debt service obligations. In this context, particular importance was attached to The Gambia remaining current in its obligations to the Fund and to the authorities' intention to accord the highest priority to building up international reserves from their present critically low level.

In sum, Directors welcomed the commitment of the authorities to adjustment. However, in view of the serious weaknesses in the economy, that commitment would have to be durable. Moreover, the achievement of the longer-term objectives of the authorities would depend both on the effectiveness of domestic demand restraint, particularly in the public sector, and on the success in diversifying the supply and export base of The Gambia, in addition to the external support needed to achieve those aims.

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

The Executive Board then took the following decisions:

Decision Concluding Article XIV Consultation

1. The Fund takes this decision relating to The Gambia's exchange measures subject to Article VIII, Sections 2 and 3, and in concluding the 1986 Article XIV consultation with The Gambia, in the light of the 1986 Article IV consultation with The Gambia conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. The Gambia maintains the restrictive exchange measures described in SM/86/216, in accordance with Article XIV, Section 2, except that the restrictions evidenced by the accumulation of commercial external payments arrears and the multiple currency practice arising from the costs to purchasers of foreign exchange of counterpart deposits required for arrears, are subject to

approval by the Fund under Article VIII, Sections 2 and 3. The Fund urges the authorities to remove these restrictions as soon as possible.

Decision No. 8397-(86/158), adopted
September 17, 1986

Stand-By Arrangement

1. The Government of The Gambia has requested a stand-by arrangement for a period of 13 months from September 17, 1986 through October 16, 1987 in an amount equivalent to SDR 5.13 million.

2. The Fund approves the stand-by arrangement set forth in EBS/86/189, Supplement 2.

3. The Fund waives the limitation in Article V, Section 3(b)(iii).

Decision No. 8398-(86/158), adopted
September 17, 1986

Structural Adjustment Arrangement

1. The Government of The Gambia has requested a three-year structural adjustment arrangement, and the first annual arrangement thereunder, under the structural adjustment facility.

2. The Fund approves the arrangement set forth in EBS/86/189, Supplement 3.

Decision No. 8399-(86/158), adopted
September 17, 1986

The Chairman noted that the authenticated request from The Gambia for a purchase transaction under the decision on the compensatory financing of export fluctuations had not yet been received. Pending its receipt, the Executive Board's approval of a purchase under the compensatory financing facility would be in principle. 1/

1/ The formal request was received on September 18, 1986, and the decision set forth in EBS/86/193, Sup. 1 (9/18/86) was adopted by the Executive Board by lapse of time (EBM/86/160, 9/19/86).

2. ZIMBABWE - 1986 ARTICLE IV CONSULTATION

The Executive Directors considered the staff report for the 1986 Article IV consultation with Zimbabwe (SM/86/200, 8/14/86; Cor. 1, 9/11/86; and Sup. 1, 9/8/86). They also had before them a background paper on recent economic developments in Zimbabwe (SM/86/228, 9/4/86).

Mr. Abdallah made the following statement:

The economy of Zimbabwe made a strong recovery in 1985 following two difficult years when the performance was severely depressed by drought, weak world demand for minerals, and shortages of imported raw materials and intermediate inputs for the manufacturing sector. In 1985 the rate of growth of GDP jumped to 6 percent, from about 1 percent in the previous year, and the improved supply conditions helped to reduce the rate of inflation from 18 percent to 10 percent. The active exchange rate policy pursued by the Government during the last two years led to an improvement in the balance of payments, and foreign reserve holdings increased to a level of two and a half months of import coverage at the end of 1985 compared with two months in the previous year.

However, the outlook for 1986 and beyond is worrisome partly due to external factors arising from the unsettled political situation in Southern Africa and partly due to internal developments. Real growth is expected to decelerate to 4 percent in 1986 while the rate of inflation is projected to rise to 15 percent owing to the depreciation of the Zimbabwe dollar and the ongoing deregulation of prices. Staff analysis of the 1986/87 budget which was announced at the end of last June, shows the fiscal deficit as rising to over 10 percent of GDP in comparison with the 1985/86 outturn of 7.6 percent. The balance of payments is expected to register a substantial deficit in contrast to the sizable surpluses which were recorded in 1984 and 1985 equivalent to SDR 95 million and SDR 81 million, respectively.

It is worth stressing that the authorities are increasingly moving toward flexible management of the economy. The comprehensive and rigid price control system is giving way to selective controls over a greatly reduced list of only those items having extensive linkages with the rest of the economy. The long time lags in getting clearance for price increases have also been reduced and consideration is being given to further streamlining of the process. The prices of a number of basic consumer items have recently been increased. Domestic production was greatly stimulated in 1985 by the relaxed attitude toward prices and by other supportive policies in addition to other favorable developments. The success of these policies has given encouragement to the authorities to carry them forward and to consider other ways of promoting further growth in the difficult period that lies ahead.

The success of the active producer prices policy has clearly been demonstrated in all sectors of the economy, especially agriculture. In the case of maize (the staple food), present production levels greatly exceed domestic consumption requirements as well as available storage capacity, and owing to problems in finding profitable export outlets, there appears to be no alternative to holding nominal producer prices constant for the third consecutive year to induce a shift to other crops such as wheat. The active producer price policy has also led to an increase in the contribution of small-scale farmers in the country's agricultural production for the market. The good agricultural output in 1985 generated strong domestic demand and was the main factor behind the expansion in manufacturing activity which occurred last year. The continuing process of price decontrol and the depreciation of the Zimbabwe dollar gave additional stimulus to manufacturing.

So far as strengthening the external sector is concerned, the country has been pursuing a policy of export promotion for some time and is negotiating a loan from the World Bank of US$125 million to further develop the sector and ease the foreign exchange constraint on manufacturing industry. Equal attention is being given to the mining sector, which contributes greatly to export earnings; in order to ensure a steady increase in the mining and production of gold, a floor stabilization price of Z$500 an ounce was recently introduced so that if the world price fell below this level, operations would not be shifted toward mining high grade ore, the usual practice in the past. The subsidy is to be deducted from the producers' earnings once the price exceeds Z$500. The policy objective was to promote steady exploitation of the gold mining sector in the interest of the country and not only the owners.

Let me now turn very briefly to the recently launched Five-Year Development Plan covering the period 1986-90, involving development outlays of Z$8,658 million. The Plan provides the medium-term policy framework for economic management and aims at achieving average real growth of 5.1 percent per annum. It envisages domestic savings as financing 67 percent of the planned investments, while external loans to the public sector will finance 25 percent. Another 6 percent of the investments are expected to be financed by grants while the remaining 2 percent is expected to be financed through direct foreign investment. A major objective of the Plan is to raise allocations for capital expenditures relative to current expenditures in each of the next five years.

Since domestic finance is expected to cover two thirds of the Development Plan, fiscal and monetary developments are therefore certain to have a major impact on it. From this point of view, the 1986/87 budget, which increases the fiscal deficit by 3 percentage points over the 1985/86 budget, is something of a setback although one which could not be avoided. The explosive sociopolitical situation in the Republic of South Africa held serious security implications for front-line states like Zimbabwe. The increases in wages and salaries which were granted to civil servants in 1985 and 1986 were made in order to restore purchasing power that had been seriously eroded in the preceding two years. But the security threat which was looming from the south could not help being a factor in the size of the award. Another adverse factor which has contributed to steadily rising allocations from the budget is the losses incurred by certain parastatals and especially the marketing boards. In the public interest the authorities have felt obliged to subsidize their losses but clearly the process cannot go on indefinitely. Accordingly, a Commission on Parastatal Organizations has recently been established to review the operations of the said parastatals and ensure that they are run more efficiently. The findings and advice of the Commission are awaited with keen interest.

Zimbabwe has pursued a fairly cautious monetary policy. The exchange rate has been managed flexibly and interest rates, while not always positive in real terms, have not been too far out of line. This stance has been facilitated by the recent policy of not resorting to bank financing but instead to finance the budget deficit through nonbank sources, mainly insurance companies and pension funds. As the tempo of private sector economic activity has been slow in recent years, public enterprises have been a more dynamic outlet for domestic credit. Under these circumstances, there has been excess liquidity in the banking system and partly due to this, and also in order to encourage private activity, interest rates have been kept relatively low. The authorities are aware that although the deficit financing has not so far imposed any strain on monetary policy, it has nevertheless absorbed national savings that could have been directed toward financing the domestic share of the Development Plan. In addition, the expected pickup in economic activity involving both the public and private sectors will, when it materializes, increase demand for credit and push up interest rates.

Finally, let me refer to the pessimistic forecasts which have been made by the staff on the country's overall balance of payments over the medium term. The authorities find that the stringent austerity measures and the pace of adjustment implied in the medium-term scenario will strain the sociopolitical fabric of the country, especially during a time when Zimbabwe is undergoing critical social adjustment. Instead, the authorities wish to develop alternative policies that will improve the capital account over the medium term, especially as the debt service is fairly high at 27.6 percent. In view of the dominance of the government sector in the economy, public investment policy will need to be critically appraised and everything done to reduce waste. The private sector will also need to be freed from unnecessary constraints in order that it may contribute to its maximum potential and attract foreign investment.

The authorities are fully conscious of all these requirements and are poised to address all of them, seeking necessary technical assistance as may be needed. They are most appreciative to the staff for the cooperation and understanding it showed during the last Article IV consultations.

Mr. Foot stated that the authorities in Zimbabwe clearly faced major challenges in their efforts to place the economy on a path of sustained growth. Many of the problems were of course structural in nature, compounded by the weakness in the price of some of Zimbabwe's major exports, but others seemed to reflect inadequate domestic policies.

The tight external position was of course one of Zimbabwe's major problems that had led the authorities to impose a rigorous system of import controls, which had in turn had adverse consequences on the growth of output, Mr. Foot observed. While the weakness of the external position was in part attributable to weak prices for major exports, as the staff had suggested, that was not the whole story. Zimbabwe's terms of trade actually appeared to have improved by about 10 percent over the past five years.

As to whether the current exchange rate was the correct one, the position was not entirely clear, Mr. Foot considered. The real exchange rate had fallen in 1986, as reported in the supplement to the staff report, although the extent of that depreciation depended partly on the measure used. For instance, the chart on page 4 of the staff report excluded the rand from the exchange rate basket; with the inclusion of the rand, as shown in the background paper on recent economic developments, the real depreciation would be considerably smaller.

There appeared to be several other reasons for considering that a further depreciation of the exchange rate might be required, Mr. Foot observed. First, export performance had been rather disappointing, there having been what the staff described as a broad-based reduction in the volume of manufactured exports. Second, even the present fairly weak external position was being maintained only with the help of controls on payments and the extensive system of foreign exchange allocations. The staff's description of the import control system in the background paper was particularly helpful in driving home the potential distortions and oddities that such a system could produce. For example, he had noted from page 56 of the background paper that the base period for allocating imports between the different commercial and industrial sectors was the share of total imports in 1964-65. On the face of it, that seemed rather surprising because there had presumably been considerable changes in the structure of Zimbabwe's industry since that time. That evasion of reality was inappropriate, to say the least. There was further indirect evidence that led him to question the appropriateness of the current level of the exchange rate in the observation in the background paper that the foreign exchange constraint had led to a sharp increase in barter and countertrade deals in recent years.

The conclusion that he drew was that there was at least good circumstantial evidence that, despite the recent depreciation, the real exchange rate remained too high and that the authorities would certainly need to continue to maintain and, if necessary, strengthen their flexible exchange rate policies, Mr. Foot went on. However, action on the exchange rate might well not be sufficient in itself to correct the strains on the external position because of the continuing pressures resulting from the large public sector deficit. It was particularly disappointing, therefore, to see the details of the latest budget, which apparently even the responsible Minister regarded as a step backward. He could accept that the budget outturn might not be as bad as forecast, but the likely reasons--including a possible shortfall in development expenditure, which had been projected to rise at what looked like an unsustainable rate--would be little cause for satisfaction.

The large fiscal deficits seen in recent years had been financeable only through administrative devices such as the requirement that most institutional investors hold at least 60 percent of their assets in prescribed securities, Mr. Foot observed. As the staff report made clear, the substantial deficits had been associated with a rising level of dissaving by the public sector. He strongly agreed with the staff that that was wholly inappropriate in light of the need to achieve the much stronger investment performance that would be required to underpin the projected rate of growth in coming years. The staff had rightly emphasized the importance of that crowding out effect in its interesting discussion of the assumptions underlying the Development Plan. The issue was all the more important because of the latest budgetary developments and because of the uncertain economic situation facing southern Africa at present. The heavy dependence of Zimbabwe on some of its major trading partners, especially for transportation, was a clear argument for caution in framing economic policies. That reality had to be squarely faced.

In seeking to strengthen the fiscal position, the main emphasis should perhaps be placed on expenditure reduction rather than on major tax increases, Mr. Foot commented, because the tax/GDP ratio did not appear to be particularly low at present. In any case, the weakness of the fiscal position in recent years seemed to have resulted mainly from the growth of current rather than of capital expenditures. In that context, the recent substantial increases in wages, while they might have increased worker morale, would presumably have added to the pressures on both public expenditure and competitiveness.

The inflationary pressures that had resulted from those wage increases had been partly suppressed by the extensive system of wage and price controls, Mr. Foot added. He noted, however, that those controls had introduced significant distortions into the economy, not least in respect of the finances of the public enterprises. In addition, if allowance was made for those effects, it would seem clear that interest rates remained negative in real terms. Together with the potentially damaging consequences for efficiency that were likely to result from the controls on the portfolio decisions of financial enterprises, and the excessive proportion of the available credit being allocated to public enterprises, that situation provided a very poor basis on which to look for the promotion of savings and productive investments that it was generally agreed would be necessary.

He had been interested by Table 3 in the background paper showing producer prices for some of Zimbabwe's major crops, Mr. Foot commented. But the table would have been even more interesting if it had compared those prices with prevailing prices not only on world markets but in the markets of Zimbabwe's neighbors. It was still not clear to him, even after having discussed the economies of other countries that produced groundnuts, what the price of groundnuts was in Zimbabwe dollars. There was a strong case for including a fully comparative table in all staff papers on countries that relied heavily on agricultural production. He would be interested in any comments by the staff on the adequacy of producer prices in Zimbabwe in general and on the merits of changing relative prices, especially those of maize and wheat.

In passing, Mr. Foot said, he wondered whether the 1987 Article IV consultation discussions might not either be delayed until information was available to the staff on the budget for the subsequent year, or be brought forward, possibly to influence the budget preparations. Apparently, the staff report for the 1986 Article IV consultation said nothing about the 1986/87 budget, which was probably too far advanced to be influenced by the staff's initial views on the economy; moreover, the Executive Board's part in the consultation came some six weeks after the budget had been announced, a not wholly satisfactory arrangement. He recognized that it was sometimes difficult to link the Article IV consultation with the appropriate budget timetable for a particular economy, but he would be interested in any thoughts that the staff might wish to offer on that matter.

In conclusion, Mr. Foot observed that the authorities of Zimbabwe had acted in various respects in the 1980s to tackle a number of severe structural problems, and the staff report showed clearly that those measures had been in the right direction. It seemed to him particularly important at the present stage to stress that progress on the budget front was the most crucial requirement, and recent developments in that respect perhaps the most disappointing.

Mr. Bethel made the following statement:

> The staff report and the background paper on recent economic developments have given a rather comprehensive review of the fiscal policies of the Zimbabwean authorities. While we agree with the general thrust of the report and endorse the proposed decision, we are concerned about the pace of adjustment required to achieve the goals outlined in the Five-Year Development Plan, 1986-90, and reiterated in Mr. Abdallah's statement.

We need not belabor in this forum the impact of the tension in South Africa and the possibility of countersanctions against Zimbabwe. Because the risks for the economy of this country are great, we would urge the authorities to take the necessary adjustment measures to consolidate and strengthen their own position so as to buffer the effects of South Africa's actions.

As indicated in Mr. Abdallah's statement, the recovery achieved in 1985 is to be commended. However, we note that while revenue and grants increased by 13 percent, total expenditure rose by approximately 16 percent. This increase represented largely disbursements on defense and to private schools. It would be appreciated if the staff could elaborate on the purposes and circumstances of the disbursements to private schools. Is the Government subsidizing private education? The increasingly burdensome support of the parastatals, along with their efficiency, should also be reviewed, and stricter control over their expenditure should be implemented.

Supplement 1 to the staff report, giving details of the 1986/87 budget, is not a welcome indication of the Government's policies. The increase in the overall budget deficit, together with increases in subsidies, seems to counteract the objectives of the new Five-Year Development Plan. We would also be interested in hearing the staff's views on timing the consultations to influence the drafting of future budgets.

While revenue collections were higher than projected in the last fiscal year, new tax reform measures indicated a possible further decrease in income. The feasibility of a reform at this time should be reviewed. The authorities should accordingly place emphasis on increased efforts at improving tax collection. However, we do encourage the retention of some flexibility in the tax system, owing to uncertainties in the economy. The political will to make the necessary adjustments must exist. The summary of the tax system in Appendix I to the paper on recent economic developments further indicates that there is scope for increasing the tax base, and we suggest that action in this area can also make allowances for tax incentives for investment.

It is estimated that less than 10 percent of the overall deficit will be covered by foreign financing. This indicates a major withdrawal of potential credit to the private sector for investment purposes and raises concern about the stability of the financial system.

In respect of the exchange rate policy, the authorities are encouraged to pursue more vigorously the more flexible policy stance adopted in 1984. A determined approach to devaluation is required so as to counteract the full effect of appreciation since 1983 and the importance of the South African rand in trade. The objective is to restore competitiveness to the exports of Zimbabwe. In addition to the liberalization of the exchange rate system, the authorities may wish to consider lifting further restrictions on the flow of capital, which would reinforce investor confidence.

Participation by the private sector and foreign investors in the development plans of the authorities is essential, whether through direct ownership or joint enterprise with Government. However, public sector involvement to the extent indicated--namely, 54 percent of total investment--should be reconsidered. The encourgement of private sector participation should be further supported by the proposed guidelines on foreign investment and the recommendations of the Commission of Inquiry into Taxation. The policy of diversification within the industrial sector is commendable and should be pursued within the guidelines on foreign investment and private sector involvement. The assistance of the World Bank and its new arm, the Multilateral Investment Guarantee Agency (MIGA), should be actively sought.

We note with interest the Government's intention to encourage self-employment. Could the staff elaborate on the forms of incentives envisaged and in what fields? While we appreciate the motives of the recent wage increase we caution the authorities to maintain controls on wages so as to avoid high unit labor costs, thereby affecting competitiveness, investment, and export potential. However, alternative approaches to maintaining competitive labor costs are the adoption of appropriate policies within the exchange system and the introduction of collective bargaining into the labor relations process. We encourage the elimination of price controls in both production and consumption as a method to ensure the efficient allocation of resources. However, such elimination must be coordinated with the gradual removal of controls on wages, thereby minimizing any inflationary effects.

The agricultural sector's importance as the major employer is both interesting and startling, accounting as it does for some 14 percent of GDP and supporting nearly 80 percent of the population. Could the staff indicate the possibilities for absorption of a larger proportion of the population in other sectors of the economy, particularly in light of the Government's encouragement of self-employment?

Finally, as I noted at the outset of this intervention, we are also concerned about the suggested pace of adjustment. While the authorities have apparently subscribed to the objectives of the second medium-term scenario presented by the staff, we feel that it is too ambitious a program to be realistic, given the constraints mentioned in Mr. Abdallah's statement. However, the required adjustments and fiscal restraint must be actively pursued, and we therefore encourage the Zimbabwean authorities to take the necessary measures as an indication of their commitment to adjustment.

Mr. Sengupta made the following statement:

Zimbabwe is one of the few African countries with a fairly diversified economy, although nearly 80 percent of the population earns its livelihood from agricultural activities.

1985 was a year of pronounced economic recovery, providing an opportunity to the authorities to put the economy on a growth path by a careful preparation and implementation of economic policies. We are heartened to see that a five-year development plan has been launched with a good performance year as the base year. An annual average growth rate of about 5 percent would be aimed at with heavy reliance on domestic savings. The targeted growth rate should be achievable, since Zimbabwe secured an average annual growth rate of 3.8 percent during the period 1981 through 1985 in spite of two successive droughts. The staff has pointed out that the targeted growth rate cannot be achieved unless the required amount of investment is mobilized through a substantial increase in savings. In this kind of an exercise, the efficiency of investment plays a critical part, and data are not firmly available in this regard. I am sure that if the Zimbabwean authorities believe that it can be done, the efficiency of investment would show some improvement even in the short or medium term. However, I would agree with the staff that savings performance would also have to be improved. As savings in most developing countries do not rise unless incomes grow, supply-side and structural measures would need to be put in place. It is this aspect which needs to receive more attention than it is given in the staff report and the background paper.

It appears from the paper that under normal weather conditions the agricultural sector of Zimbabwe produces more than enough food crops, livestock, and dairy products to meet domestic consumption requirements. The authorities have also increased the producer prices of maize, wheat, soybeans, sorghum, groundnuts, and cotton in recent years, thereby giving incentives to farmers to produce more. As noted in the background paper, and as Mr. Abdallah has pointed out in his statement, the price incentives seem to have led to a large contribution to output by small farmers. I wonder if the staff could tell us how far the institutional changes, including services, such as the provision of inputs and new technologies, have played a part in improving agricultural output. Price incentives alone could not have done the trick, as shown by the case of wheat, whose output has been short of domestic demand in spite of higher producer prices and improved weather conditions during the last two years. In any case, the authorities would need to ensure that agricultural incomes rise and stimulate the output of manufactured products.

The development of the manufacturing sector seems to hinge on foreign exchange availability, which in turn depends on export capability and on improvements in infrastructure, such as energy and transportation. Apart from domestic demand stimulus, exports undoubtedly need to rise. In Zimbabwe, exports play a vital role, and we welcome the recent negotiation of an export promotion loan from the World Bank.

The staff report devotes much attention to fiscal and monetary policies, exchange rate policy, and the medium-term outlook. The supplement to the staff report shows that the 1986/87 budget estimate increases the fiscal deficit to GDP ratio by 3 percentage points to 10.6 percent. Revenue growth is estimated to decelerate due to a marked reduction in the tax burden; the reason for this is not clear. Is the objective to improve tax collection, the profitability of companies, and increase the public's disposable income? How much of the anticipated income growth this year will have a favorable impact on revenues this year? And are there any lagged income growth effects on revenues?

The supplement to the staff report describes the increase in expenditure estimates. In this connection, it mentions wage increases as one of the causative factors. But on page 13 of the staff report, such wage increases were regarded as consistent with the policy of wage restraint. While statistically these increases might have caused expenditure overshooting, they are appropriate from the points of view of economic efficiency and the evolution of demand. Increased defense expenditures seem to be due to the security implications arising from what Mr. Abdallah called "the explosive sociopolitical situation" in South Africa. Subsidies have gone up, after a year of total stagnation in 1985/86. But even at the estimated level, the rise in subsidies was lower than in 1983/84 and 1984/85. This shows that the trend in subsidy payments is moderating. We welcome in this context the announcement about the setting up of a commission on parastatal organizations to review the operation and recommend ways of improving the efficiency of parastatals.

One of the areas where performance was commendable was monetary policy. The rate of broad money growth of 16 percent in 1985 was marginally lower than the rate recorded in the previous year. Data for the first quarter of 1986 showed a decline in broad money. Net domestic credit also fell in the first quarter of 1986, with claims on government and the public sector recording considerable declines; claims on the private sector showed a small increase during this quarter. Given these trends, it is puzzling to note a reference to monetary growth as an important problem area and a contributor to inflation. Deposit rates also do not appear to be as unattractive as they were made out to be. Otherwise, how do we explain the substantial rise in quasi-money, especially "other term deposits?" It is of course true that there is a need to have a measure of flexibility in the conduct of interest rate policy in order to ensure that resource allocation is appropriate, but on the whole, the conduct of policy appears to be in the right direction.

The exchange rate policy was flexibly pursued, and the real effective exchange rate has depreciated since January 1983. However, the depreciation contributed to inflation, and it has unfortunately not improved export competitiveness. The staff suggests that the depreciation should be accelerated and accompanied by import liberalization, a recommendation with uncertain effects. Moreover, the staff has not provided a detailed defense of its position.

The medium-term scenarios show that with higher growth rates and higher import volumes, the debt service ratio would decline over a five-year period because of large net capital flows and improved export earnings. I am not sure whether export earnings could grow at an annual average of 10.5 percent, given the weakness in commodity prices. It is, however, possible to get the same numbers through careful planning of imports to suit the needs of development.

What strikes us most in the staff report is the extraordinarily moderate policy stance that shows clear evidence of a gradual shift to liberalization, with a view to improving the growth rate and making efficient use of resources. Such an adjustment process, with a bit of luck and determined implementation on the fiscal side, should augur well for Zimbabwe.

Mr. Polak made the following statement:

Five years have passed since independence, and although the earliest of these were characterized by a prospering economic situation, thereafter the situation deteriorated, and all economic data now point to very sluggish development. This is due partly to adverse exogenous developments but partly also to failing economic policies.

The authorities are now formulating their plans for the next five years, and the staff has presented a convincing case that the main goals of the authorities--securing a high rate of growth while improving the external position--are fully attainable, if the right kinds of policies are pursued. It is therefore very unfortunate that the new budget, described in the supplementary staff paper, is wholly out of line both with the authorities' own medium-term goals and with the staff's advice. Correctly, the staff singles out budgetary problems and the system of import controls as the most important elements that at present impede favorable economic developments.

The budget deficits of the public sector have over the last few years continued to be very large. Since the peak in the drought year of 1982, these deficits have hardly fallen below 10 percent of GNP. As a consequence, the Government is absorbing savings that would otherwise have been available for investment, which in turn would raise future growth rates. Moreover, the Government is relying heavily on administrative schemes to get its deficit financed, such as the requirement that banks and insurance companies invest in government securities at negative real interest rates. It seems, moreover, that one source of cheap, albeit questionable, financing is coming to an end, namely, the blocked accounts of nonresidents, a purely inflationary form of financing in all but name. Continuing large budget deficits could therefore in the future even more openly influence monetary developments and thus inflation.

Looking at the causes of the deteriorating government finances, it is clear that expenditures have not been kept under adequate control. This is especially true of the wage bill and the continuing large increase in transfers. In addition, subsidies to the parastatal sector, caused largely by inadequate pricing policies, have kept rising. In this respect, particular attention is called to the position of the marketing boards, all of which have continued to incur losses.

A second area of concern is insufficient export growth, which has led the authorities to implement a system of strict administrative controls on imports in contrast to the hope of import liberalization that was held out in earlier consultations. The resulting limited availability of imports has impeded economic growth and export growth. In this respect, the decision of the authorities to pursue a more aggressive exchange rate policy is to be welcomed. From the staff report it is clear that some progress has already been made. However, owing mainly to the devaluation of the South African rand, more needs to be done. This is clear both from the losses of the marketing boards, and the apparent excess demand for imports.

A third area of concern seems to be the heavy reliance on administrative measures to control wages and prices. The problem with this is that price controls all too often are inadequate in adjusting prices to changes in economic conditions and put pressure on enterprises' profitability. This in turn is not conducive to stimulating investment and economic growth. While I welcome the recent streamlining of administrative procedures, I urge the authorities to move ahead decisively in this area, and to remove most of the remaining price controls.

More flexibility is needed in wage policy. I concur with the staff's observation that collective wage bargaining may be useful in order to transfer the responsibility for wages to employers and employees, where it properly belongs. I would like to stress, however, that in the interim price differences should be taken into account, and a more decentralized approach to wage determination could be helpful. However, this does not relieve the Government of its task of setting an example through a more moderate approach to the wage bill in the government sector.

The authorities have been following a prudent external debt policy. At present, the debt burden seems to be manageable. Nevertheless, the amortizations due this year and next, will put further pressure on the balance of payments, and international reserves can be expected to decrease to a precariously low level.

Unlike many other African countries, Zimbabwe has a fairly diversified and efficient economy and is not yet plagued by external debt servicing problems. Indeed, the staff has shown the courage to suggest an alternative scenario that would lead to a larger debt by 1990 than was likely under the present set of policies. In Zimbabwe, good results can be obtained quickly if the right policies are pursued. In view of the tight external situation expected this year and next, the country could greatly benefit from Fund assistance, as the staff has demonstrated in its informative scenario. However, the new budget seems to make that virtually impossible, as it is clearly counter to the staff's advice. It contains once again excessively large increases in the wage bill and in subsidies to the parastatals, and, most unfortunately, measures to reduce the tax burden. I urge the authorities to follow up on the staff's advice by reducing their budget deficit as a matter of urgency, by pursuing an active exchange rate policy, and by allowing market forces to play a larger role in the economy. A stand-by arrangement and a structural adjustment arrangement would be highly appropriate.

Mrs. Walker made the following statement:

The outlook for Zimbabwe's economy in 1986 and beyond is not without problems, but on the whole we believe the problems that exist are manageable. Sources of concern clearly are the projected rate of growth in real GDP and the prospects for the balance of payments. Attention should be focused on financial policies of the Government and on removing rigidities in the economy.

The creation of the Five-Year Development Plan for 1986-1990 is a positive step. However, we are concerned that attainment of the Plan's objectives may not be possible without higher levels of investment than are currently expected. We concur with the staff's suggestion that there is an urgent need to improve the savings performance of the Government and parastatals, particularly in order to contribute to the financing of the planned increase in investment. I note, however, that the authorities believe that the improvement in the savings performance could take place at a somewhat slower pace, and the new budget unfortunately goes in this direction. Understandably, there are always constraints to implementing reductions in government expenditures, but I urge the authorities to do as much as they can to reduce expenditures as quickly as possible, particularly in the area of wages and transfers to parastatals.

The investment plan calls for 54 percent of investment to be undertaken by the public sector and only 46 percent by the private sector. We believe that private sector investment should be encouraged and that a reduction in the overall deficit of the Government, particularly through reductions in expenditure, is essential to free up savings to finance private sector investment, not only in the industrial sector, which is largely in private hands, but in other sectors where practicable. The revised foreign investment guidelines could also contribute to increased private sector investment, and I would appreciate staff comment on their potential for helping to attract more foreign investment.

In general, the financial performance of the parastatals has been weak, and they are a serious drain on government resources. The agricultural marketing authority appears to be in the worst shape, owing to the subsidies provided to producers and consumers, but others, including the oil distributor, have incurred losses. A reduction in the losses of these enterprises is needed, and I urge the authorities to take the measures recommended by the staff in this regard. We welcome the establishment of a commission on parastatal organizations to review the operations of these industries and will be very interested in receiving the detailed study.

Credit to the parastatals clearly must be limited if credit to the private sector is to be large enough to allow for the encouragement of private economic activity envisaged under the Development Plan. In this regard, it would also be essential for interest rates to increase in real terms.

The system of price controls is cumbersome and causes distortions in the economy. We urge the authorities to remove commodities subject to administrative approval and reduce the time lag for approval of others, while noting, of course, the progress that has been made thus far.

Increasing the prices of certain products or services provided by parastatals will also be an important ingredient in the improvement of the parastatals. Producer price flexibility has positively influenced growth in the agricultural sector. In particular, the contribution of small-scale farmers to agricultural production has increased, and we encourage continued flexibility in producer prices.

Employment prospects in Zimbabwe do not appear strong over the medium term, according to the staff report, in spite of a projected upturn in economic growth and the Government's efforts to encourage self-employment. New employment opportunities should emerge as the private sector expands and as rigidities in the labor and product markets are reduced.

In the external sector, I note the substantial export restrictions and complex system of foreign exchange allocation. Furthermore, in spite of the depreciation of the exchange rate, exports appear not to have responded as much as could be expected. Trade liberalization and an accelerated and more flexible exchange rate policy should help to alleviate some of the balance of payments pressures.

In addition, I agree with the staff and others that other efforts will need to be made, including an improvement in government savings to help promote investment, an easing of import restraints, greater flexibility in the administration of price controls, and incentives for foreign and domestic investment.

In the end, we believe the authorities are equipped to meet the challenges ahead and provide an improvement in the balance of payments and growth prospects.

Mr. Orleans-Lindsay made the following statement:

During the last Article IV consultation discussion, Directors cautioned that unless the Zimbabwean authorities took measures to ease the foreign exchange constraint and to remove the structural impediments to growth, the recovery of the economy might not be self-sustaining. Indeed, the staff report clearly indicates that the encouraging recovery of the Zimbabwean economy that began in late 1984 and continued in 1985 appears to have slowed considerably, with GDP growth for 1986 projected at slightly less than 3 percent compared with 6 percent in 1985. The deterioration in the budgetary situation intensified in recent months. In the external sector, the current account deficit has been maintained at around 3 percent of GDP during the past two years, down from 8.5 percent of GDP in 1983, although only because of the imposition of restrictions on payments and transfers and a severe compression of imports. External debt service payments have continued to increase. These developments are indeed worrying, and the Zimbabwean authorities need to re-examine their policy options and make substantial changes that could alleviate the serious economic and financial difficulties that have been projected for the immediate future as well as for the medium term.

Since I agree with the general thrust of the original and the updated staff appraisal, I will briefly comment on the fiscal sector where the 1986/87 budget projects a further worsening of the Government's overall financial position. This seems to go against the medium-term objectives that the authorities have set. The projected increase in the deficit by 3 percentage points of GDP over the outturn for the preceding fiscal year does not appear sustainable and is a great cause for concern, given the need for a substantial mobilization of resources to finance the Five-Year Development Plan. In this connection, it will be crucial for the successful financing of the Plan that the Zimbabwean authorities adopt a new fiscal strategy that places emphasis on controlling the growth of expenditure through tight restraint on transfers to parastatals and limits on increases in the wage bill. A policy of general wage flexibility in Zimbabwe is called for, as suggested by the staff. The rate of increase in expenditure on goods and services should also be curtailed in order to release financial resources for private investment. Unless the authorities take steps to stimulate domestic savings to levels that can adequately finance the Plan, it is unlikely that the growth targets could be achieved. Revenue-raising measures are urgently called for, and in this connection I would be grateful if Mr. Abdallah or the staff could provide any additional information on the report of the commission on taxation.

On the timing of the Article IV consultation cycle, I would with Mr. Foot that the authorities might wish to consider a change that would enable them to take advantage of the Board's comments on economic and financial developments in Zimbabwe. Policy recommendations and suggestions could then be noted for incorporation in the Government's budget proposals at the appropriate time. I support the proposed decision.

The staff representative from the African Department explained that the mission had been timed in response to a request by the authorities, who had wished to benefit from the staff's views in the preparation of the budget, which had been well under way. The staff would have preferred an earlier discussion. The usual dilemma was that either the staff would have no information on the budget if it arrived too soon, or if it arrived late, when all the necessary information would be at hand, it would have no input. In the event, he considered that the timing of the mission had been appropriate. Conflicting views had been expressed by the various participants in the discussions in preparation for the budget, and the staff's views might have been helpful, even though they had not carried enough weight to affect the budget outcome.

As the staff report made clear, Zimbabwe had followed a fairly reasonable policy on producer prices, the staff representative continued. The problem, to which there was no apparent solution at present, concerned the price of maize relative to the prices of other products. For three successive years, the price of maize had not been increased, but there had been substantial increases in the prices of other agricultural products, including wheat. The price of wheat had been increased by 6 percent for 1986/87, following increases of 14 percent in both 1985/86 and 1984/85. The problem was complicated by the division of the agricultural sector into two separate parts: 70-80 percent of the output was produced by

10,000 large, modern farms, on 20-25 percent of the fertile territory; the remaining 20 percent was produced by a few million farms on the 70 percent of the land that was not fertile. In addition, and particularly before 1979/80, the output of maize for trading purposes was produced by the large, modern farms, whereas for the past three or four years, the Government had been supporting development in the rural agricultural sector by means of higher producer prices but also, as Mr. Sengupta had suggested, by technical assistance and the commercialization of the output of small farms. The problem had become one of changing relative prices to encourage large farms to produce other crops and small farms to produce some maize. The process was not easy and would take time.

The exchange rate did pose a problem of some significance, the staff representative considered. For a number of years, export performance had been poor, especially with respect to products that were sensitive to relative prices. Imports had had to be compressed greatly through quantitative restrictions. At present, the demand for foreign exchange was almost twice the supply, based on the demand of importers, who could request allocations only for imports of specific products, mainly a limited number of inputs and raw materials, and capital goods. Thus, all the signs of an overvalued exchange rate were present.

At first sight, the increase in wages of 3-10 percent had not seemed excessive, the staff representative remarked. The fiscal problem had become apparent only when the budget revealed a large increase in current expenditure, not only on the increased wage bill but also on military expenditure. Moreover, tax rates had been reduced at the same time, with the result that the budget deficit had increased from 7 1/2 percent to 10 percent of GDP. The staff had not been able to see the one available copy of the report on taxation.

Monetary policy was not a major problem, although interest rates were too low, the staff representative stated. There was a range of interest rates, some being market determined and some not. A large amount of financial resources took the form of blocked accounts, which carried a rate of interest of 4 percent; the rate of inflation was currently 15-16 percent. Admittedly, the funds in those blocked accounts could not be moved, but the rate of interest on them was highly negative.

The authorities were trying to attract foreign investment, the staff representative commented. Whether or not they would be successful remained to be seen. Some multinationals might choose to invest in Zimbabwe rather than in South Africa, although given the small size of the domestic market they would do so only to the extent that they could export a substantial proportion of their output. The issue then became one of the exchange rate and the availability of inputs, quite apart from the important question of where export markets would be found. South Africa had been the main export market for manufactured goods, and Zimbabwe's exports were currently going through South Africa to the rest of the world. Whether that movement of exports would continue would depend to a large extent on political developments in southern Africa.

The subsidization of private education took the form of the payment of teachers' salaries, the staff representative explained. A large part of the educational system was in private hands, and the Government was saving money by paying salaries and avoiding the cost of building and maintaining public schools. The large increase in the Government's contribution resulted from an increase of 200-300 percent since 1979/80 in the proportion of the population having access to primary education. There was a built-in increase in the Government's expenditure on education because the impact of its policy was beginning to be felt in the secondary and technical schools, where the costs were much higher.

The impediment to the absorption of the bulk of the population into the modern sector, as opposed to the agricultural sector, stemmed again from the structure of the manufacturing sector; highly developed manufacturing and mining sectors were basically in private hands and employed only a small part of the population. The main objective of the Development Plan was to increase the rate of growth in the modern sector in order to absorb more labor, calling for capital formation on a large scale. The necessary investment in capital stock in the manufacturing, mining, and modern agricultural sectors would not be forthcoming if most savings were absorbed by the public sector. At best, the solution could only be a partial one, perhaps a slowing of growth in the rate of unemployment. The authorities were expecting to develop cooperatives in the agricultural sector while changing the system of education, which was oriented largely to supplying labor to the modern sector that could not provide enough employment opportunities.

Mr. Abdallah remarked that a consultation mission to Zimbabwe--or to Kenya, for that matter--should not be timed too close to the date on which the budget would be announced, either from the point of view of the member country or that of the Fund staff, particularly if unpopular measures were to be announced. The missions should take place sufficiently in advance of the budget announcement, say when the figures for the first ten months of the fiscal year were available. If that happened, the discussions on the budget would be more productive.

There was a qualitative difference in the response of wheat and maize output to incentives, Mr. Abdallah explained. Wheat growing was a large-scale commercial operation, whereas maize could be planted by a small farmer on one quarter of an acre, if only for subsistence purposes, and the productivity of various small farms did not vary greatly. Consequently, it was difficult to raise the output of wheat, but not at all difficult to encourage maize output; there were surpluses of maize.

The authorities were aware, and had so indicated to the staff, that the larger budget deficit appeared to be a backward step, Mr. Abdallah continued. At the same time, they took the Five-Year Development Plan seriously and were committed to achieving the targeted growth rate of 5 percent. Consequently, they would be looking critically at current expenditures, including social spending. But there was another aspect to consider. The authorities noted that the budget outturn in the two preceding fiscal years had been better than they expected, the staff projection of a deficit of 7.9 percent of GDP having been exceeded by just 0.3 percent. Therefore, they hoped that the budget deficit in the current fiscal year would be less than projected, at around 9 percent of GDP instead of 10 percent of GDP. Moreover, the overall economic performance had not been as disappointing from the point of view of the budget, the balance of payments, employment, and economic growth. The optimism of the authorities was in fact justified by the stronger base of economic activity throughout the country than in many other African countries: the cost structure in Zimbabwe was not wasteful; the people were prudent; the potential for tourism existed; and South Africa was not the only market for exports, given the potential offered by the preferential trading area in central, eastern, and southern Africa that was not being fully exploited at present owing to the balance of payments difficulties in the region. The communications and transportation network would have to be geared to developing that larger market, in the event that access through South Africa was no longer possible.

The staff representative from the African Department added that the budget had been made public eight weeks after the consultation discussions. Therefore, the authorities should have had time to consider the staff's views. Although the budget outcome had been better than expected in the previous fiscal year, the overall deficit had decreased only because public investment had been substantially below the budgeted amount. Current expenditures had been above the amount provided initially in the budget. From that standpoint, it would not be surprising if the overall deficit was less than 10.6 percent in the current fiscal year; nor would it be surprising if it was above the 6.5-7 percent in the budget. The performance of the Zimbabwean economy had certainly not been totally disappointing. The development of the agricultural sector, outside of the 10,000 modern farms, had been proceeding remarkably well. Relations between the authorities and the private sector, including the manufacturing and mining sectors, had been good. Pricing policies, while not sufficiently flexible, had been satisfactory on the whole. The economy was well diversified and well managed and had considerable potential, which was perhaps why some of the authorities' policies were disappointing to the staff.

South Africa was not the only market for Zimbabwe's exports, although it took about 40 percent of the exports of manufactured products, the staff representative said. It would not be easy to expand exports to other neighboring countries quickly enough to offset a sizable decline in exports to South Africa. Efforts were being made to expand exports to Europe and to OECD countries generally, but transportation was a problem, particularly through Mozambique owing to security problems.

In response to a question from Mr. Vasudevan, the staff representative from the African Department said that it was difficult for him to know why the authorities had decided to reduce the tax rates in the 1986/87 budget; he had not yet had an opportunity to see the relevant report or to discuss the matter with the authorities. To some extent, the authorities might have been attempting to repeat the increase in domestic demand for all goods and services that had been stimulated at the end of 1984 and in 1985 by improved weather. At present, economic activity was declining. It was hard to see how a reduction in taxes could help, given the balance of payments situation.

Mr. Abdallah commented that the timing of the mission had been set by the authorities and should certainly make it possible for the budget to be discussed before expenditure decisions were taken. At the same time, he saw no major difference in principle on the direction of policy between the staff and the authorities. If anything, the difference of view concerned the perception of how well the economy had been performing. The major issue in late 1987/88 would be the progress made under the Development Plan. In that connection, the advice of the World Bank and of the Fund staff might be sought, especially if it became necessary to increase investments to achieve the objectives of the Plan, in which event additional financial resources would have to be found, as the Fund staff had suggested.

The Chairman made the following summing up:

Executive Directors agreed with the thrust of the appraisal in the staff report for the 1986 Article IV consultation with Zimbabwe that the economic situation continued to give cause for concern. After the marked recovery of late 1984 and 1985, which was largely the result of the return of adequate rainfall, the economy seemed to be returning to the previous path of very slow growth. Investment in the productive sectors remained low, and exports continued to stagnate. Debt service payments were now absorbing a large proportion of foreign exchange earnings and the reduction in imports of intermediate inputs was limiting economic activity. Thus, the internal and external constraints on balanced growth were increasing, and their resolution constituted a major challenge to the authorities.

Directors noted the publication of the Development Plan for 1986-90, with its ambitious growth target, and they emphasized that there was an urgent need to take major policy decisions to raise domestic savings, including the reduction of government dissavings, and to increase the efficiency of investment if the plan was to have a chance of succeeding. They viewed the persistence of a large budgetary deficit as the root cause of most of the current economic difficulties. They noted that both the Central Government and the limited public sector deficits had increased in 1985/86 and that there would be a further increase in the overall budgetary deficit of the Central Government of some 3 percentage points to over 10 percent of GDP in 1986/87. Government dissavings could be equivalent to nearly 7 percent of GDP in 1986/87. Such a budget was disappointing. It could only aggravate existing imbalances, particularly with regard to prices and the balance of payments. It threatened to crowd out the private sector and make it impossible, or very difficult, to increase investment as envisaged in the Plan. Directors therefore urged the authorities to take action to reduce the deficit, particularly by restraining current expenditure, especially the wage bill and current transfers. They stressed the need to reduce the operating deficit of the parastatals through price increases and improvements in efficiency, and welcomed the establishment of a government commission to that effect.

Directors also stressed the need to continue following cautious monetary policies in order to achieve a decline in the rate of inflation. In addition, there was a need for a redirection of credit away from parastatals and from the government sector as a whole toward the private sector. They further noted that real interest rates, which are currently negative, should be allowed to rise to positive levels in the medium term to reflect the expected tighter liquidity situation.

Directors observed that the release of more resources for investment should be accompanied by measures aimed at increasing production and investment incentives. They noted that agricultural producer prices had generally been adequate, but that there had been delays in adjusting other prices. Directors therefore urged the authorities to introduce greater flexibility with regard to these other prices by reducing the number of commodities subject to ministerial or administrative control, and streamlining approval procedures. They also pointed to the need for a more flexible mechanism for establishing wage rates that would allow for greater differentiation among sectors and firms.

Directors noted that the recent overall balance of payments surpluses had been achieved mainly through a compression of imports through the use of quantitative restrictions. They felt that these restrictions aggravated the misallocation of economic resources and hindered private investment. In view of the current poor performance and outlook for exports and the balance of payments in 1986 and beyond, Directors urged the Zimbabwean authorities to continue to follow a flexible exchange rate policy, allowing the real effective exchange rate of the Zimbabwe dollar to depreciate and to introduce a phased program for the liberalization of imports. Directors also urged the authorities to improve the economic climate for foreign investment. Indeed, they observed that in Zimbabwe, with its strong resource base and diversified economy, good results would soon follow from the firm pursuit of appropriate policies and the necessary encouragement of the private sector. Budgetary restraint was of primary importance if those aims were to be achieved.

It is expected that the next Article IV consultation with Zimbabwe will be held on the standard 12-month cycle, it being understood that the timing of these consultations may have to be adjusted so that the mission can have some input into the discussions on the annual budget preparation.

The Executive Board took the following decision:

1. The Fund takes this decision relating to Zimbabwe's exchange measures subject to Article VIII, Section 3, in concluding the 1986 Article XIV consultation with Zimbabwe, in light of the 1986 Article IV consultation with Zimbabwe, conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. As described in SM/86/228, Zimbabwe continues to maintain restrictions on payments and transfers for current international transactions in accordance with Article XIV, Section 2, except that the multiple currency practice arising out of the 20 percent fee on sales of foreign exchange for holiday travel is subject to approval under Article VIII, Section 3. The Fund encourages the authorities to take measures that will permit the elimination of these restrictions as soon as possible.

Decision No. 8401-(86/158), adopted
September 17, 1986

3. IMF WORKING PAPERS - ESTABLISHMENT OF DOCUMENT SERIES

The Executive Directors considered a matter concerning the establishment of a new series of documents entitled IMF Working Papers (WP) (Sec. Circ. No. 86/96, 8/20/86; and Sup. 1, 8/29/86).

Mr. Kafka explained that he had requested that the matter be brought to the agenda, rather than approved by a lapse of time decision, because it had seemed helpful to give the Board an opportunity to comment on the establishment of a new series of documents, or what was perhaps the transformation of one series into a different one.

Among the aspects that deserved consideration, Mr. Kafka mentioned, the first was the possible budget implications. The question was whether the documents in the WP series should be distributed more widely outside the Fund than the Departmental Memoranda (DM) series had been. Should the papers be made available only to entities in whose studies the Fund staff also had an interest, or should they be made generally available, and if so, would any charge be made? It seemed that many members of the scholarly community would be interested in the Fund staff's work, whereas the contrary might not be true. One of the best forms of propaganda for the Fund to engage in might be to provide its staff studies--possibly without charge--so that the academic community would realize that the Fund's work went beyond preaching austerity to its members.

Mr. Foot commented that his authorities at the Bank of England had been confronted about three years previously with the type of considerations to which Mr. Kafka had alluded. The Bank of England had been preparing to issue development papers, with the objective of achieving a certain favorable publicity but without being bound by the author's comments and without incurring a great deal of expense. It had been decided to produce the series in a much cheaper, less durable, but more visible form than the official publications of the Bank of England as a way of demonstrating that the documents concerned constituted a working paper. The distribution of the new series, apart from a system of exchange similar to that of the Fund, had been tackled by publishing an occasional list of the papers produced in the series in the Quarterly Bulletin of the Bank of England, with an offer to provide a free copy to anyone who requested one. For certain papers, a two- or three-line summary of the content had been printed. Presumably only those who were really interested would take the trouble to request a paper. The procedure had worked quite satisfactorily from that point of view.

Mr. Polak remarked that he had understood the proposal more as an attempt to reorganize some of the series of documents issued by the Fund. In his view, Staff Papers was the main organ of Fund propaganda. In fact, most DMs usually ended up being edited for publication in Staff Papers. Therefore, he would not favor promoting the new series of Working Papers beyond the distribution proposed in Secretary's Circular No. 86/96, which was in line with present practice for distributing DMs, in order to avoid too much competition with or comparison between Staff Papers and the new Working Papers.

Mr. Alfidja inquired how the World Bank handled the distribution and publication of similar series.

The Deputy Director of the External Relations Department said that the idea was to issue an informal, plainly produced document, with a low-key distribution, very much along the lines described by Mr. Foot. With a view to avoiding competition with Staff Papers, the distribution would be confined to specialists, who were likely to comment on the paper before it appeared in published form. One advantage of the proposal was that it would cut the time lag between issuance of a working paper prepared by the staff and its later publication. The quality of the papers selected for publication might in fact improve.

The list of institutions on the distribution list would be quite restricted, the Deputy Director explained. At present, there were 255 institutions in 45 countries on the list; the number might be reduced if some institutions no longer wished to receive the papers, but it could also be increased, if there was sufficient interest. The Fund was not bound by reciprocity agreements with other institutions.

The periodic distribution of abstracts was the other form of distribution contemplated, the Deputy Director noted. Fliers could be distributed with Staff Papers containing a number of abstracts of the papers then available, and it would be incumbent upon any individual to request a copy.

No charge was being proposed in the first instance, the Deputy Director of the External Relations Department said. However, the costs of the new system of distribution would be monitored closely, and if the demand warranted it, and the expense seemed likely to be significant, a service charge of say, $3-5 might be imposed.

Mr. Templeman stated that in general he supported the proposal, which seemed to be a way of modestly increasing knowledge of what the Fund was doing and thinking. The costs of producing the present DM series must be minimal. Although the new series should also not be costly if only 255 copies were to be issued at the outset, the matter should be kept under review.

With respect to the reference in the staff paper to retaining the DM series for research papers containing sensitive or confidential material, Mr. Templeman asked how often it would be necessary to issue DMs for that purpose.

The Deputy Director of the External Relations Department responded that such material was seldom contained in research papers, and DMs would rarely be necessary.

The World Bank had previously issued working papers in a regularly published series that it had promoted strongly, the staff representative noted. Since the recent establishment by the World Bank of two new periodic publications, the manner of distributing the working papers had been changed by limiting the list of recipients and publishing extracts along the lines proposed for the new Fund series of working papers.

In response to a question by Mr. Salehkhou, the Deputy Director of the External Relations Department said that he would provide a list of the 45 countries on the list to receive the new papers.

Mr. Vasudevan remarked that if the Fund was propagating ideas and at the same time eliciting comments on its working papers, it should not be too concerned with the costs. With respect to the distribution list, he asked whether it would include institutions only or individuals as well. Perhaps individuals would be expected to request papers if they were interested in the abstracts to be published in Staff Papers.

The Deputy Director of the External Relations Department explained that the regular distribution lists would be limited to institutions. Individuals would be expected to request specific papers, notifications of their existence appearing in fliers to be distributed with Staff Papers, and not in the latter publication itself.

In response to a further remark by Mr. Vasudevan, the Deputy Director confirmed that papers would continue to be sent to individuals known to be interested in the subject to enable views to be exchanged before the papers were finalized.

In response to a comment by the Chairman, the Deputy Director of the External Relations Department said that institutions on the distribution list did provide the Fund with copies of their own papers.

Mr. Polak commented that he wished to raise a point that was only indirectly related to the matter on discussion but provoked by it. He suggested that the staff should make a survey of Executive Directors to determine the extent of interest in continuing to receive the papers in the financial series on foreign exchange and gold prices.

The Executive Directors agreed that the new series of Working Papers (WP) should be established.

APPROVED: May 27, 1987

JOSEPH W. LANG, JR.
Acting Secretary