FOR AGENDA

EBS/85/239

CONFIDENTIAL

October 1, 1985

To: Members of the Executive Board

From: The Acting Secretary

Subject: Mauritania - Staff Report for the 1985 Article IV Consultation and Review Under Stand-By Arrangement

Attached for consideration by the Executive Directors is the staff report for the 1985 Article IV consultation with Mauritania and a review under its stand-by arrangement. Draft decisions appear on pages 26 and 27.

This subject is tentatively scheduled for discussion by the Executive Board on Monday, October 28, 1985, which results in a slight shortening of the normal circulation period of four weeks.

Mr. Artus (ext. 7676) or Mr. Marciniak (ext. 8516) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

Att: (1)

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

MAURITANIA

Staff Report for the 1985 Article IV Consultation and Review Under Stand-By Arrangement

Prepared by the African Department and the Exchange and Trade Relations Department

(In consultation with the Fiscal Affairs, Legal, and Treasurer's Departments)

Approved by G.E. Gondwe and S. Kanesa-Thasan

October 1, 1985

I. Introduction

A staff mission consisting of Messrs. Artus (head-AFR), Hill (AFR), Marciniak (AFR), Regling (ETR), and Ms. Casaromani (secretary-AFR) visited Nouakchott during the period June 27-July 11, 1985 to conduct the 1985 Article IV consultation discussions and the first review under the 12-month stand-by arrangement which ends in March 1986. Policy discussions were held principally with Lieutenant Colonel Anne Amadou Babaly, Minister of Finance and Commerce; Mr. Mohammed Ould Lekhal, Minister of Planning and Territorial Management; and Mr. Dieng Boubou Farba, Governor of the Central Bank of Mauritania. The discussions were concluded at Fund headquarters during the period August 12-16, 1985, when the staff met with a Mauritanian delegation headed by the Minister of Finance and Commerce. In accordance with the stand-by arrangement, the first review focused on the implementation of the financial program in the first semester of 1985 and the policies and performance criteria for the second semester.

The 12-month stand-by arrangement for Mauritania, approved by the Executive Board on April 12, 1985, is for an amount of SDR 12 million, equivalent to 35.4 percent of Mauritania's quota of SDR 33.9 million (EBS/85/41 and Supplements 1 and 2). To date, Mauritania has purchased the first two installments of SDR 2.4 million each; the first purchase was made after Board approval of the arrangement and the second following confirmation that the end-March 1985 performance criteria had been met. The remaining purchases are scheduled to be made in three quarterly amounts of SDR 2.4 million; the next purchase can be made upon the completion of the first review under the program. With one minor exception, explained in Section II.2 below, Mauritania was in compliance with the performance criteria for end-June. As of end-June 1985, Mauritania's total use of Fund credit amounted to SDR 29.4 million

(86.7 percent of quota), all under tranche policies. If all scheduled repurchases and all scheduled purchases under the current stand-by arrangement are made, Mauritania's outstanding use of Fund credit will reach the equivalent of 79.4 percent of quota by end-March 1986 (Table 1).

The last Article IV consultation discussions were held in Nouakchott during the period August 2-19, 1984. The staff report for the consultation (SM/84/257) and the report on recent economic developments (SM/84/262) were considered by the Executive Board on December 10, 1984. On that occasion, Directors noted with deep concern the extremely difficult economic and financial situation which Mauritania had been facing for a number of years and suggested that a fundamental reorientation of economic and financial policies was needed. They urged the authorities to adopt an appropriate exchange rate policy, limit investment expenditure to external financing available on concessional terms, strengthen the overall budgetary position, eliminate outstanding domestic and external payments arrears, relax price controls, and take measures to improve the operating and financial performance of the public enterprises.

Mauritania continues to avail itself of the transitional arrangements of Article XIV. A number of selected economic and financial indicators are presented in Appendix I. A summary of the policy measures in the 1985 program and their implementation is shown in Appendix II. A letter from the Governor of the Central Bank of Mauritania summarizing developments in the first semester of 1985 and policies for the second half of 1985 is included in Appendix III. Summaries of Mauritania's relations with the Fund and the World Bank Group are provided in Appendices IV and V, respectively. The basic data table and a note on statistical issues are included in Appendices VI and VII, respectively.

II. Background and Recent Economic Developments

After many years of generally inadequate economic policies, Mauritania is now in the first phase of an adjustment effort aimed at eliminating the internal and external imbalances built up during the 1970s and early 1980s.

1. The buildup of imbalances, 1970-83

During the period 1970-83, Mauritania's production base contracted significantly. Adverse climatic conditions, together with inadequate producer prices, reduced the traditional production of cereals on nonirrigated land from about 100,000 tons in the late 1960s to less than 25,000 tons during the 1982/83 (June-May) crop year, while the production on irrigated land rose slowly from 3,000 tons in the late 1960s to less than 10,000 tons in 1982/83. In the mining sector, iron

Table 1. Mauritania: Use of Fund Credit During the Stand-By Arrangement Period

	Outstanding at beginning of arrangement	1985 April-June	1985 July-Sept.	1985 Oct.-Dec.	1986 Jan.-March	Total
		(In millions of SDRs)				
Transactions under tranche policies (net)						
Purchases		4.8	--	4.8	2.4	12.0
Ordinary resources		4.8	--	4.8	2.4	12.0
Borrowed resources		--	--	--	--	--
Repurchases		3.1	3.4	3.3	3.0	12.8
Ordinary resources		2.2	2.3	2.4	2.0	8.9
Enlarged access resources		--	--	--	--	--
Supplementary financing		0.9	1.1	0.9	1.0	3.9
Transactions under special facilities (net)		--	--	--	--	--
Purchases		--	--	--	--	--
Repurchases		--	--	--	--	--
Total Fund credit outstanding (end of period)	27.7	29.4	26.0	27.5	26.9	
Under tranche policies	27.7	29.4	26.0	27.5	26.9	
Under special facilities	--	--	--	--	--	
		(As percent of quota)				
Total Fund credit outstanding (end of period)	81.7	86.7	76.7	81.1	79.4	
Under tranche policies	81.7	86.7	76.7	81.7	79.4	
Special facilities	--	--	--	--	--	

Source: IMF, Treasurer's Department

ore production stagnated between 8 and 10 million tons, with dips below 8 million tons in 1977-78 and 1982-83, while the production of copper ceased in 1978. In the manufacturing sector, attempts to set up relatively large enterprises failed, and small- and medium-scale enterprises together never employed more than 1,000 workers. In the fishing sector, the authorities adopted a new policy in 1979 aimed at increasing their control of fishing activities in Mauritania's coastal waters. However, by 1983 the net foreign exchange receipts from fishing remained small, largely because of the dependence of the sector on foreign equipment and seamen.

The contraction of the production base took place despite large inflows of foreign resources and high investment rates from 1974 onward. During 1974-83, Mauritania received an average of SDR 93 million a year in public transfers, as well as SDR 105 million a year in (net) foreign loans, mostly on concessional terms. While some of these resources were used for food imports, as well as the financing of military expenditures during Mauritania's involvement in the conflict over the Western Sahara in 1976-79, most of them were invested. During 1974-83, the ratio of fixed investment to GDP averaged nearly 33 percent, one of the highest in the world; however, the yield on investment was extremely small.

Some factors responsible for this low yield, e.g., the climatic change which contributed to the failure of many agricultural projects, were largely exogenous; others, however, were endogenous--misallocation of resources and poor management of projects. As much as 40 percent of new investment was devoted to transport infrastructure, with many projects in this area chosen on the basis of other than strict production considerations. Another 20 percent was devoted to publicly managed industrial ventures, including a petroleum refinery and a sugar refinery, which proved unviable and which were subsequently closed.

Along with the contraction of the production base, there emerged large fiscal and balance of payments imbalances. By 1983, the Government's consolidated overall fiscal deficit (on a commitment basis and including external grants) was equivalent to 11.2 percent of GDP (Table 2). Excluding external grants, the deficit amounted to 21.4 percent of GDP. This large fiscal imbalance, added to the effects of a decline in the real price of iron ore and a policy of real exchange rate appreciation, was reflected in an even larger balance of payments imbalance. By 1983, the deficit of the current account (including public transfers) was equivalent to 28.2 percent of GDP. Excluding public transfers, the deficit was 38.3 percent of GDP. By end-1983, the outstanding foreign debt was about US$1.2 billion, equivalent to 164 percent of GDP.

Table 2. Mauritania: Consolidated Government Fiscal Operations, 1981-85 1/

	1981	1982	1983	1984 Estimates Previous 2/	1984 Estimates Revised	1985 Program 2/	1985 Projection
				(In million of ouguiyas)			
Total revenue and grants	11,700	11,838	13,317	17,348	16,323	21,532	19,532
Budgetary revenue	6,665	7,211	8,935	10,436	10,296	12,451	12,348
Grants	5,035	4,627	4,382	6,912	6,027	9,081	7,184
Budgetary	1,370	325	160	82	63	--	103
Extrabudgetary 3/	3,665	4,302	4,222	6,830	5,964	9,081	7,081
In kind 4/	(1,146)	(1,181)	(1,674)	(2,413)	(2,150)	(3,403)	(2,616)
Project	(1,465)	(1,671)	(1,259)	(2,786)	(2,999)	(3,387)	(3,000)
Other	(1,054)	(1,450)	(1,289)	(1,631)	(815)	(2,291)	(1,465)
Total expenditure and net lending	13,357	16,302	18,156	21,433	19,944	23,708	21,708
Current expenditure	9,579	10,881	12,791	13,716	12,499	17,697	15,424
Budgetary 5/	(7,828)	(8,427)	(10,294)	(10,620)	(10,463)	(12,003)	(12,003)
Extrabudgetary 6/	(1,751)	(2,454)	(2,497)	(3,096)	(2,036)	(5,694)	(3,421)
Investment expenditure	3,685	5,354	5,247	7,575	7,303	5,866	6,139
Budgetary	(475)	(612)	(704)	(564)	(583)	(706)	(706)
Extrabudgetary	(2,761)	(4,565)	(4,077)	(6,063)	(5,791)	(5,160)	(4,773)
Special accounts	(449)	(177)	(466)	(948)	(929)	(--)	(660)
Net lending	93	67	118	142	142	145	145
Overall fiscal deficit (Commitment basis)	-1,657	-4,464	-4,839	-4,085	-3,621	-2,176	-2,176
(excluding grants)	(-6,692)	(-9,091)	(-9,221)	(-10,997)	(-9,648)	(-11,257)	(-9,360)
Change in payments arrears (+ increase)	436	498	449	649	649	-6,647	-8,371
External	(...)	(...)	(273) 7/	(514) 7/	(514)7/	(-5,905)8/	(-7,671) 8/
Domestic	(...)	(...)	(176)	(135)	(135)	(-742)	(-700)
Overall fiscal deficit (-) (cash basis)	-1,221	-3,966	-4,390	-3,436	-2,972	-8,823	-10,547
Financing	1,221	3,966	4,390	3,436	2,972	8,823	10,547
Foreign borrowing (net)	3,844	5,411	4,316	3,313	3,324	-1,081	-1,067
Drawings 3/	4,096	5,826	5,071	4,732	4,540	3,249	3,249
Budgetary	(2,800)	(2,932)	(2,253)	(1,455)	(1,748)	(1,476)	(1,476)
Project	(1,296)	(2,894)	(2,818)	(3,277)	(2,792)	(1,773)	(1,773)
Amortization 3/	-252	-415	-755	-1,419	-1,216	-4,330	-4,316
Domestic (net)	-2,623	-1,445	74	123	-352	--	--
Banking system	703	426	1,458	--	-125	--	--
Other 9/	-3,326	-1,871	-1,384	123	-227	--	--
External debt relief and exceptional assistance	--	--	--	--	--	--	11,657
Rescheduling	(--)	(--)	(--)	(--)	(--)	(--)	(8,858)10/
Exceptional assistance	(--)	(--)	(--)	(--)	(--)	(--)	(2,799)11/
Financing gap (surplus -)	--	--	--	--	--	9,904	-43
Memorandum items:				(In percent of GDP)			
Budgetary revenue	18.4	18.6	20.7	22.6	22.3	24.1	23.4
Expenditure and net lending	37.0	42.0	42.2	47.8	43.2	45.8	41.2
Current expenditure	(26.5)	(28.0)	(29.7)	(30.6)	(27.1)	(34.2)	(29.3)
Investment expenditure	(10.2)	(13.8)	(12.2)	(16.9)	(15.8)	(11.3)	(11.6)
Overall fiscal deficit (commitment basis)							
Including grants	4.6	11.5	11.2	9.1	7.8	4.2	4.1
Excluding grants	18.5	23.4	21.4	24.5	20.9	21.8	17.7
Financing gap	--	--	--	--	--	19.2	-0.1

Sources: Data provided by the Mauritanian authorities; and staff estimates.

1/ Including expenditure financed directly from abroad and therefore not recorded in Treasury accounts.
2/ As indicated in EBS/85/41.
3/ As recorded in the balance of payments.
4/ Foreign-financed food aid, including food aid with counterpart recorded under special accounts.
5/ Including interest due.
6/ Equivalent to the counterpart of extrabudgetary grants (excluding project grants), less expenditure under special accounts (counterpart of food aid).
7/ Arrears on interest only.
8/ Settlement of external debt service arrears, including amortization.
9/ Determined as a residual.
10/ Interest and amortization due in 1985 as well as arrears outstanding at the end of 1984.
11/ Including grant from Saudi Arabia of US$30 million (UM 2,019 million).

2. The shift toward adjustment, 1984-85

Although fiscal and monetary policies were tightened in late 1983 and in 1984, the adjustment effort remained limited. In particular, the decline in the consolidated fiscal deficit excluding external grants was only marginal because of a sharp rise in extrabudgetary investment expenditure financed by external grants. Furthermore, the adjustment effort did not include a significant change in the exchange rate, and, therefore, it failed to tackle the major supply-side problems. There was a brief period from January to May 1984 during which the exchange rate was allowed to depreciate, but this was immediately followed by a new phase of appreciation (see Chart). The result was a structure of domestic prices that hindered economic activity in the three main sectors producing internationally traded goods, namely fishing, agriculture, and mining.

Even though the current account position improved significantly in 1984, the overall external position remained weak. The current account deficit (including public transfers) declined from the equivalent of 28.2 percent of GDP in 1983 to 19.6 percent of GDP in 1984, mainly because of a fall in imports of equipment for the Guelbs iron ore project. However, the balance on nonmonetary capital worsened markedly as amortization payments rose, while disbursements for the Guelbs project fell. The overall deficit (before debt relief) rose from 11.3 percent of GDP in 1983 to 15.5 percent of GDP in 1984. By end-1984, gross official international reserves had declined to SDR 82.7 million, the equivalent of two months of imports of goods and nonfactor services. Accumulated external arrears had reached SDR 118.8 million, of which SDR 104.8 million was for medium- and long-term public and publicly guaranteed debt.

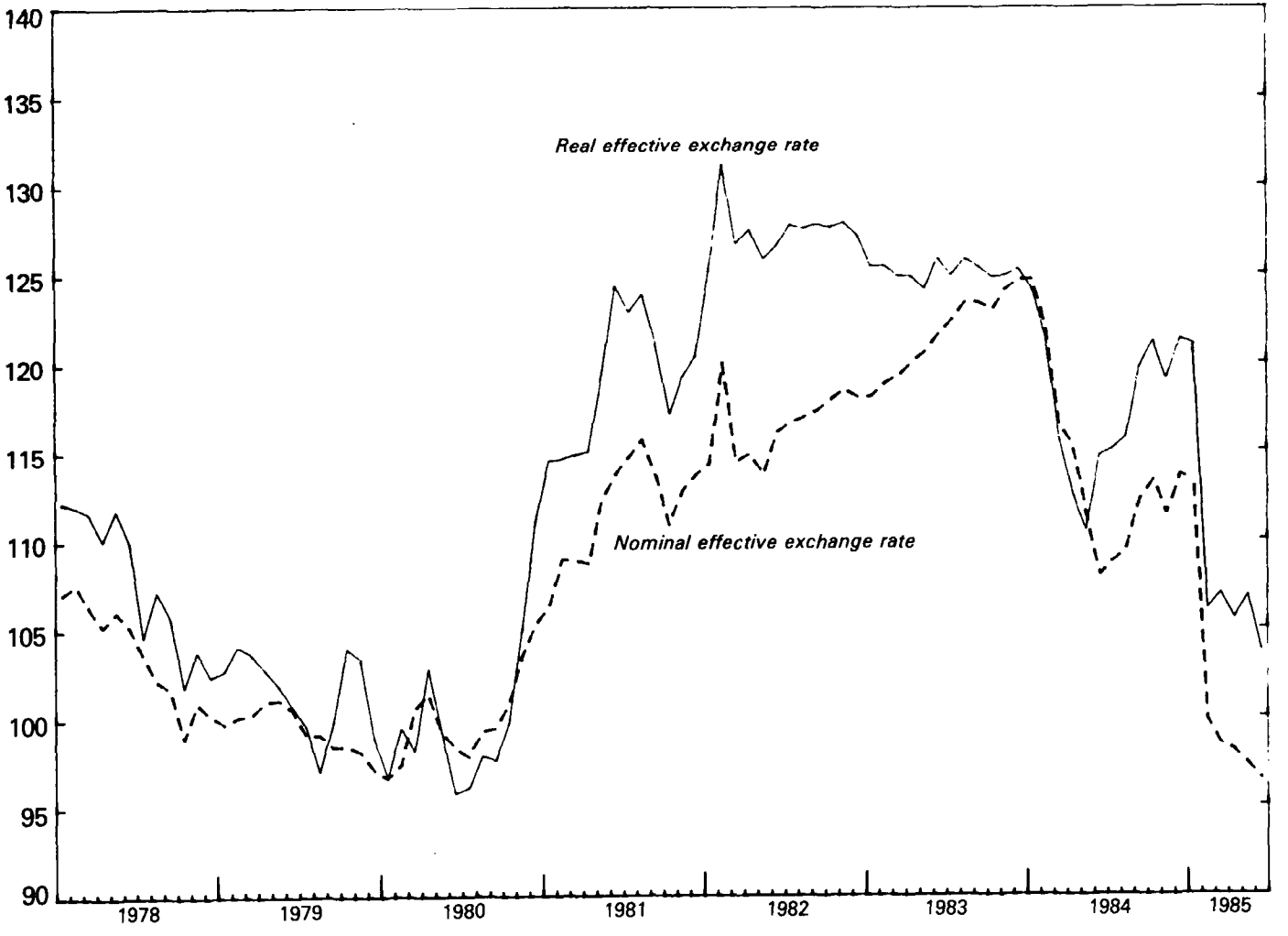
In early 1985, the Government adopted a more comprehensive and strengthened adjustment program, which is supported by the current stand-by arrangement. For 1985, the major objectives of the program are to reduce the current account deficit of the balance of payments (including public transfers) to 14 percent of GDP, to limit the inflation rate to 12 percent, and to achieve a rate of economic growth of 3 percent. More fundamentally, however, the aim of the program is to initiate the much needed longer-run process of adjustment. The objectives of the program are to be achieved through (1) a substantial devaluation of the ouguiya; (2) increases in domestic prices of internationally traded goods; (3) an intensification of the effort to rehabilitate public enterprises; (4) a drastic cut in public investment expenditure financed through foreign borrowing in conjunction with an improvement in investment decision making; (5) improvements in tax administration and continued controls over current outlays; (6) a further tightening of credit policy; and (7) external debt relief. Further actions required to carry out the longer-run process of adjustment are to be elaborated in an Economic and Financial Recovery Plan for 1985-88, which is being prepared with the help of the World Bank.

CHART 1

MAURITANIA

NOMINAL AND REAL EFFECTIVE EXCHANGE RATES, 1978-JUNE 1985

(1980 = 100)



Sources: IMF, International Financial Statistics; and staff calculations.

The main elements and objectives of the 1985 program are described in Table 2 (consolidated government fiscal operations), Table 3 (balance of payments), and Table 4 (monetary aggregates).

All the key actions envisaged thus far in the program have been taken as scheduled (see Appendix II). All the performance criteria for the end of March and the end of June were respected, except for the elimination of guaranteed commercial arrears. This criterion was, however, observed two weeks after the end-June deadline.

III. Report on the Discussions

The discussions with the authorities covered recent economic and financial developments in conjunction with the Article IV consultation and the first review under the stand-by arrangement.

1. Results of the gap-fill exercise

A major issue in the discussions was the outcome of the gap-fill exercise. The Mauritanian authorities stated that, although rescheduling arrangements between Mauritania and its creditors and negotiations concerning exceptional assistance had not yet been finalized, on the basis of firm commitments (including the result of the Paris Club meeting), the authorities considered it likely that the financing gaps for both the balance of payments and the Treasury would be covered. As a result of the Paris Club agreement in April 1985 and the subsequent acceptance by other creditors (excluding multilateral institutions and bilateral Arab funds) of terms similar to those granted by the Paris Club, about UM 11 billion (US$134 million) of arrears and debt service due in 1985 on account of medium- and long-term public and publicly guaranteed debt would be eventually rescheduled. This amount would be equivalent to almost 80 percent of all outstanding arrears at the end of 1984 and more than 50 percent of debt service due in 1985. For the 1985 budget, the positive effect of the debt rescheduling was estimated at UM 8.9 billion (US$112 million).

In addition to the debt rescheduling, Mauritania had received exceptional financing from several countries and Arab organizations, including a grant of US$30 million (UM 2,019 million) from Saudi Arabia, which was received in January 1985 and was used largely for budgetary purposes, including the settlement of government domestic arrears. Altogether, the authorities hoped that the gap-fill exercise would contribute an amount of UM 12 billion (US$156 million) to the Treasury. Taking into account recent revisions to the stock of external arrears, the estimated budget deficit in 1985 could be slightly overfinanced (Table 2). Similarly, with respect to the balance of payments, the gap-fill exercise would yield US$198 million, thus slightly exceeding the revised financing gap forecast for 1985 (Table 3). The authorities

Table 3. Mauritania: Balance of Payments, 1981-85

	1981	1982	1983	1984 Estimates Previous 1/	1984 Estimates Revised	1985 Program	1985 Projection
				(In millions of SDRs)			
Trade balance, f.o.b	-99.0	-168.3	-58.8	-104.6	-8.1	-20.2	10.6
Exports	229.7	216.5	295.0	284.9	286.6	323.9	316.8
Imports	-328.6	-384.8	-353.8	-389.5	-294.7	-344.1	-306.3
Services (net)	-104.1	-151.2	-194.5	-205.9	-205.1	-155.8	-171.6
Interest	-38.0	-39.6	-47.4	-53.4	-50.2	-53.1 2/	-50.3 2/
Other	-66.1	-111.6	-147.1	-152.5	-154.9	-102.7	-121.3
Transfers	68.0	49.7	45.7	80.8	75.0	88.4	78.4
Private	-17.5	-27.9	-28.3	-24.9	-22.5	-21.0	-19.1
Public	85.5	77.6	74.0	105.7	97.6	109.4	97.5
Current account balance							
Including public transfers	-135.1	-269.8	-207.6	-229.7	-138.2	-87.6	-82.6
Excluding public transfers	-220.6	-347.4	-281.6	-335.4	-235.8	-197.0	-180.1
Nonmonetary capital (net)	111.6	163.7	124.7	128.5	31.8	15.8	6.1
Disbursements	114.3	171.7	169.4	175.9	103.5	82.4	74.8
Principal repayments	-58.5	-43.4	-54.6	-67.5	-69.4	-76.6 2/	-71.2 2/
Other capital 3/	55.8	35.4	9.9	20.1	-2.3	10.0	2.5
Overall balance before debt relief	-23.5	-106.1	-82.9	-101.2	-106.4	-71.8	-76.5
Accumulation of arrears (+ indicates an increase)	-19.4	16.2	19.7	37.9	41.8	-113.5 4/	-113.3 5/
Interest	-5.1	6.7	7.7	12.9	18.0	-34.1	-44.3
Principal	-14.3	9.5	11.9	25.0	23.7	-79.2 4/	-69.0 5/
Reserve changes (- indicates an increase)	-11.3	64.2	37.1	34.1	35.3	--	--
Central Bank	-2.0	28.0	27.1	35.6	29.2	--	--
Of which: net purchases from the Fund	(4.4)	(13.9)	(-4.3)	(-9.4)	(-9.0)	(-12.2) 6/	(-2.6) 7/
Deposit money banks	-9.2	36.2	10.0	-1.5	6.1	--	--
External debt relief and exceptional assistance	54.2	25.8	26.1	29.2	29.4	...	198.3
Financing gap (surplus -)	--	--	--	--	--	197.3	-5.8
Current account deficit				(In percent of GDP)			
Including public transfers	21.2	39.9	28.2	33.5	19.6	14.1	12.3
Excluding public transfers	34.7	51.3	38.3	48.9	33.4	31.6	26.9

Sources: Data provided by the Mauritanian authorities; and staff estimates.

1/ As indicated in EBS/85/41.
2/ Including debt service on the financing of the gap.
3/ Including direct investment, private and short-term capital, valuation adjustments and errors and omissions.
4/ Including SDR 20 million in arrears on commercial credit.
5/ Including SDR 8.5 million in arrears on commercial credit.
6/ Excluding purchases from the Fund in 1985.
7/ Including purchases from the Fund in 1985.

Table 4. Mauritania: Monetary Aggregates, 1981-85

(In millions of ouguiyas; end of period)

	1981	1982	1983	1984		1985							
						March		June		September		December	
				Prog.	Actual	Prog.	Actual	Prog. 1/	Actual	Prog.	Revised	Prog.	Revised
Foreign assets (net)	-737	-4,375	-6,598	-9,768	-9,614	-11,637	-11,306	-11,637	...	-11,870	-11,691	-12,103	-11,511
Central Bank	1,639	77	-1,533	-4,176	-3,749	-4,975	-4,409	-4,975	...	-5,075	-4,559	-5,174	-4,191
Deposit money banks	-2,376	-4,452	-5,065	-5,592	-5,865	-6,662	-6,897	-6,662	...	-6,795	-7,132	-6,929	-7,320
Domestic credit	13,557	16,441	18,084	19,642	19,762	19,850 2/	19,319	20,050 2/	19,854	20,450	20,650 2/	20,660	20,850 2/
Claims on Government (net)	3,257	3,683	5,141	5,142	5,016	5,142 2/	4,785	5,142 2/	4,914	5,142	5,016 2/	5,142	5,016 2/
Central Bank	3,537	4,435	5,404	5,405	5,294	5,405	5,038	5,405	...	5,405	5,279	5,405	5,279
Deposit money banks	-1	-406	-72	-55	-55	-55	-69	-55	...	-55	-55	-55	-55
Post Office and Treasury	-279	-346	-191	-208	-223	-208	-184	-208	...	-208	-208	-208	-208
Claims on rest of economy	10,300	12,758	12,943	14,500	14,746	14,708	14,534	14,908	14,940	15,308	15,634	15,518	15,834
Central Bank	--	--	--	--	--	--	--	--	...	--	--	--	--
Deposit money banks	10,014	12,351	12,736	14,293	14,539	14,501	14,327	14,701	...	15,101	15,427	15,311	15,627
Treasury	286	407	207	207	207	207	207	207	...	207	207	207	207
Money and quasi-money	9,431	9,245	10,084	11,000	10,992	11,208	11,854	11,408	...	11,808	11,876	12,018	12,563
Money	7,654	7,135	8,089	9,300	9,290	9,478	9,925	9,645	...	9,983	10,033	10,161	10,618
Currency outside banks and Treasury	2,678	2,950	3,024	3,330	3,307	3,394	3,599	3,454	...	3,575	3,571	3,639	3,780
Demand deposits	4,845	4,049	4,941	5,870	5,891	5,982	6,195	6,087	...	6,301	6,362	6,413	6,733
Post Office	131	136	124	100	92	102	131	104	...	107	100	109	105
Quasi-money	1,777	2,110	1,995	1,700	1,702	1,730	1,929	1,763	...	1,825	1,843	1,857	1,945
Long-term borrowing by banks	201	74	116	104	100	104	18	104	...	104	104	104	104
Other items (net)	3,188	2,747	1,285	-1.230	-944	-3,099 3/	-3,859 3/	-3,099 3/	...	-3,332 3/	-3,021 3/	-3,565 3/	-3,328 3/

Source: Data provided by the Mauritanian authorities.

1/ As indicated in EBS/85/41.
2/ Performance criterion.
3/ Including valuation impact.

stated that, given the short-term nature of some of the loans and the difficult situation expected to prevail over the next several years, any overfinancing that might materialize would be used to reduce the Government's debt to the Central Bank and to build up external reserves.

2. Production and investment

The Mauritanian representatives stated that, even though production during 1985 suffered from the continuation of drought during the 1984/85 agricultural crop year, favorable developments in the fishing and mining sectors and the gradual rehabilitation of certain public enterprises could lead to an increase in real GDP of about 2.5 percent in 1985, against the decline of 0.5 percent in 1984. While it was still too early to say, they anticipated that the recent heavy rainfalls could lead to an even better performance in 1986.

The authorities stated that the 1984/85 cereal crop was about 30,000 tons, covering only 10 percent of national consumption. However, thanks to food aid and the organization of an efficient food distribution system, there had not been any severe shortages; it was expected that about 50 percent of the domestic cereal requirement would be met through foreign-financed food aid in 1985, while commercial imports would account for 40 percent. The authorities were much more optimistic with regard to the 1985/86 harvest. They stated that, if the favorable rate of rainfall observed so far in July-August 1985 continued until October 1985, cereal production could rise to about 60,000 tons, and the livestock population could begin to recover.

Production in the fishing sector was likely also to be significantly higher in 1985 than in 1984, largely because of the abnormally low fish catch in the first half of 1984, resulting from the dispute over fishing agreements. In this context, the authorities stressed that control over the country's fishery resources had been substantially improved since the new fishing policy was initiated in 1979. However, they admitted that the fishery sector's contribution to economic growth and employment creation still fell short of expectations, and that the policies implemented so far had been only moderately successful in reducing private capital outflows and tax delinquency. To increase net foreign currency inflows and tax revenues from the fishing sector, the authorities created in late 1984 a parastatal responsible for exporting the fish landed in Nouadhibou. Although the new parastatal had contributed positively in these areas, the authorities acknowledged that this was not a long-run solution and that they would have to implement a medium-term strategy aimed at reinforcing Mauritania's control and management of its fisheries resources and at making onshore activities more competitive. To make this possible, the authorities would have to rectify the problems of high cost of water and energy supplies in

Nouadhibou, inadequate management, and the lack of qualified workers. The recovery plan for 1985-88, currently being prepared with the help of the World Bank, was addressing these problems.

Another favorable development in 1985 was the further recovery of the iron ore sector. The representatives of SNIM, the iron ore mining company, expected the volume of exports of iron ore to exceed the 9.5 million tons of 1984 because European steel plants were reconstituting their inventories. In recent months, iron ore prices had been stable in terms of foreign exchange and had risen sharply in terms of ouguiyas as a result of the recent depreciation of the ouguiya. These developments, as well as cuts in operating costs resulting from a wage freeze and a comprehensive rehabilitation project undertaken with the help of the World Bank, were leading to a marked improvement in SNIM's financial position. SNIM representatives indicated that the Guelbs mine had begun production in early 1985 and that its iron ore was in high demand because of good processing characteristics. However, they were conscious of the fact that the longer-run outlook for the world iron ore market was not good and that the Guelbs mine involved higher production costs than the Kedia mine, which was nearly depleted. This implied that SNIM would have to make further progress in improving productivity in order to remain competitive and generate enough internal savings to continue the development of the Guelbs mine.

The authorities stated that, in addition to the rehabilitation of SONADER and SNIM, they were continuing their efforts to rehabilitate the whole public enterprise sector. A number of public enterprises had already been closed down or transferred to the private sector, and a major rehabilitation project had been agreed with the World Bank in early 1985 for the electricity and water supply company (SONELEC), the Nouakchott port authority (EMN), and the post and telecommunications agency (OPT). Although government subsidies to commercial public enterprises were not sizable, in most cases public enterprises had failed to settle their tax liabilities and to service their foreign debt, while the Government had often failed to pay for the utilities and services provided by the public enterprises. As a result, substantial interlocking debts had accumulated. In early 1985, the Government and the public enterprises agreed on a timetable to settle these debts.

Turning to investment, the authorities stated that public investment, which still accounted for about 90 percent of total fixed investment, had been exceptionally high in recent years, mainly as a result of the Guelbs mining project and the Timbédra-Néma road. Following the completion of these projects, public investment was expected to decline sharply in 1985. Disbursements declined from US$190 million in 1983 to US$161 million in 1984 and were expected to decline further

to about US$126 million in 1985, or well within the limit of US$130 million envisaged in the Fund-supported financial program for 1985. As a result, the amount of new foreign loans fell from US$181 million in 1983 to US$106 million in 1984 and US$74 million in 1985. Mauritania's new public investment policy emphasized rehabilitation projects and other projects that would rapidly contribute to domestic production and exports. In 1985 nearly 44 percent of disbursements were for rural development, mainly the development of irrigation. The authorities stated that this new orientation would be continued and that substantial progress had been made already in devising sectoral strategies and project selection in the context of the preparation of the Economic and Financial Recovery Plan for 1985-88 which is to be submitted to a Consultative Group meeting in late November 1985.

3. Wages and prices

The Mauritanian representatives stated that, in spite of the recent exchange rate depreciation, inflation had been kept largely under control by limiting increases in wage rates in the government sector and in public enterprises to about 2 percent and by maintaining a restrictive credit policy. In fact, the consumer price index (CPI) had risen at an annual rate of less than 5 percent during the first half of 1985. The authorities acknowledged that a number of administered prices for imported goods had not been fully adjusted to reflect the depreciation. However, they explained that profit margins on most of these goods had become excessive by 1984 because administered prices had not been reduced during the period 1981-84 to reflect the sharp appreciation of the ouguiya in real terms and the decline in world market prices of products such as petroleum, tea, and sugar.

In principle, the authorities concurred with the need to adjust administered prices promptly in line with changes in economic costs, including those resulting from exchange rate movements. In this regard, they had just decided to review the appropriateness of administered prices of imported goods and, in the future, to allow these administered prices to reflect exchange rate adjustments within four weeks. In addition, to diminish government control over pricing, the authorities intend to reduce the number of goods subject to administered prices. For cereals, however, the authorities argued that an exception had to be made on humanitarian grounds. They explained that, since February 1985, the Government had been cushioning consumers from the price increases that took place under the program by distributing free of charge about 70 percent of food aid. The staff stressed that this practice could threaten the program's objectives and advised the authorities to adopt a more cautious approach to free food distribution, including the establishment of clear and narrower eligibility criteria. The authorities concurred and pointed out that efforts were under way with the assistance of donors to establish a list of indigents and to promote food-for-work programs.

While acknowledging that inflation was largely under control, the staff expressed the view that the CPI was not fully reliable. In particular, it pointed out that movements in the individual components of the CPI were extremely erratic. This erraticism plus a 15 percent decline in the housing component in June resulting from new rent regulations made it difficult to assess inflationary developments. Nevertheless, after adjustment for rent regulations and seasonal factors, the rate of increase of the CPI during the first half of 1985 appeared to be roughly in line with the 12 percent rate assumed in the program. Net of the direct effects of the 16 percent devaluation, the underlying rate of inflation was probably in the 6 to 8 percent range. The authorities acknowledged that the data used for the calculation of the CPI in recent months needed to be reviewed.

4. Fiscal policy

The staff noted that a major objective of the Fund-supported adjustment program for 1985 was to reduce the consolidated government deficit on a commitment basis, including grants, to UM 2.2 billion (4.2 percent of GDP). Excluding grants, the deficit was to be reduced to UM 11.3 billion (21.8 percent of GDP). The Treasury deficit, which excludes most expenditures financed directly abroad by external loans and grants, was to be reduced to UM 0.4 billion (0.8 percent of GDP). To achieve these objectives, the program envisaged a sharp cut in extrabudgetary investment financed by foreign loans. It also envisaged that budgetary revenue, after increasing by 15 percent in 1984, would rise by an additional 20 percent in 1985 (based on revised figures for 1984), largely as a result of the devaluation of the ouguiya. The growth in current budgetary expenditure, which had been limited to only 2 percent in 1984 (revised data), would increase by 15 percent in 1985 to allow for the effect of the devaluation. Preliminary results for the first few months of 1985 indicated that extrabudgetary investment and loans and budgetary outlays were within the limits of the program. On the other hand, budgetary revenue appeared to be running significantly below the program targets, owing in part to deficiencies in tax administration.

In response to the staff's observations, the authorities stated that the fiscal efforts undertaken in 1985 should be viewed as part of a longer-term adjustment process. The marked reductions in the consolidated government deficit (including grants) and in the Treasury deficit in 1984 already reflected measures taken to broaden the tax base and to enhance the revenue elasticity of the tax system, and to restrain the growth in current expenditure. To achieve further progress in the adjustment process in 1985, the original budget adopted in January converted various excise taxes from specific to ad valorem rates. After concluding the preparation of the Fund-supported adjustment program for 1985, the authorities issued a revised budget at the end of March, which incorporated the targets of the program. In the revised

budget, salaries of the civil service, which had been reduced in real terms by about 13 percent during the period 1983-84, were allowed to increase by only 2 percent in nominal terms, and military expenditures were frozen at the 1984 level. Moreover, to maintain a freeze on the level of public employment in 1985, as envisaged in the program, the Government would be obliged to offset the expected recruitment of about 800 school graduates educated abroad or in the national professional schools by the same number of employment terminations.

In the discussions, there was a general consensus that the overall fiscal adjustment was generally on track and that the objectives of the program for the whole of 1985 were achievable. The authorities acknowledged that revenues from taxes on business profits and on imports, in particular, had fallen short of the program objectives during the first few months of 1985. However, they stressed that this was only due to a temporary lag in tax collection and that the shortfall would be made up in coming months. Extrabudgetary grants and expenditure were substantially below the amounts envisaged under the program, mainly because of a decline in the value of food aid. Thus, the consolidated fiscal deficit excluding grants would be smaller than envisaged. The staff stressed that a greater administrative effort to collect taxes was needed during the second half of the year to ensure that the revenue target in the program for 1985 was reached.

With regard to government payments arrears, the Mauritanian representatives stated that all outstanding domestic arrears, estimated at UM 700 million (revised) at the end of 1984, had been eliminated by the end of June 1985, that is, three months ahead of the end-September deadline prescribed in the program. As a result of the favorable outcome of the gap-fill exercise, the authorities did not expect any difficulty in eliminating all external payments arrears by end-September 1985, as targeted in the program.

5. Monetary and credit policy

The authorities stressed that during the first half of 1985 credit expansion had been extremely stringent: net credit to the Government had declined by 2 percent, credit to the rest of the economy had risen by less than 2 percent, and total domestic credit had remained about constant. As a result, the credit expansion had been kept within the program's credit ceilings (Table 4). Credit expansion had in fact been tighter than initially envisaged under the program because the credit ceilings for end-March and end-June had been determined on the basis of credit projections at end-December 1984, but actual total credit for end-December 1984 had been UM 120 million higher than initially forecast.

In addition, according to a recent study undertaken by the Central Bank, the capitalization of interest on nonperforming loans represented nearly half of the expansion of domestic credit to the nongovernment sector in the first half of 1985, so that the amount of liquidity creation resulting from the credit expansion had been very small.

The authorities added that, during most of 1984, private importers and public enterprises had managed to escape the effects of the restrictive credit policy by having recourse to credits from foreign banks, with Mauritanian commercial banks as guarantors or domiciliary banks. In many instances, private importers had subsequently defaulted on their loans, which had then been assumed by the Mauritanian banks. The Mauritanian banks, in turn, had not only accumulated nonperforming loans but also external arrears. To tighten its control on credit and on the banking sector, since late 1984 the Central Bank had required prior authorization by its credit department for any external commercial credit. The result had been a sharp cut in recourse to the facilities of foreign banks. As envisaged in the program, the Central Bank had also conducted a comprehensive survey of external commercial arrears in April 1985, which had identified SDR 13.5 million of nonguaranteed commercial credits and SDR 2.8 million of guaranteed commercial credits. These figures compare with the respective figures of SDR 16.9 million and SDR 3.1 million tentatively estimated in early 1985 (see EBS/85/41). 1/ As already noted, all arrears on guaranteed credit were eliminated through rescheduling in mid-July 1985. It was envisaged that 40 percent of the arrears on nonguaranteed credit would be repaid in 1985.

As a result of the accumulation of nonperforming loans, Mauritania's banks were facing a severe lack of liquidity. The authorities had attempted to solve the liquidity crisis through increases in banks' equity, further private participations in their capital, and negotiation of several moratoria. However, they acknowledged that an in-depth rehabilitation of the banking sector was needed and noted that a study financed jointly by the World Bank and the Arab Monetary Fund had already been initiated. The results of the study were expected to be available at end-October 1985, and will be reviewed at the time of the second review under the program.

Interest rates, which had remained fixed since 1980, were raised across the board by 2 percentage points in February 1985, as required under the program. Rates paid on deposits now ranged from 7 to 11 percent, while lending rates ranged from 8.5 to 16 percent. The authorities agreed to keep interest rates under review so as to maintain real positive interest rates. They indicated that it was too early to

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1/ The decline in the estimate of arrears on guaranteed credit is due to the reclassification of a loan of SDR 0.3 million, whose validity is now in litigation in the Spanish courts.

appraise the impact of the new interest rates but, according to preliminary information, they had not resulted in increased bank deposits. They considered that the spread between cash and time deposits was insufficient and that the interest rate of 7 percent on cash deposits should be reduced in order to promote time deposits. However, changes in the interest rate structure would await the conclusion of the study on the banking sector.

6. External position

The authorities expected to achieve the program's balance of payments targets for 1985, in particular the reduction in the current account deficit (including public transfers) from a revised 19.6 percent of GDP in 1984 to 14.1 percent of GDP in 1985. Actual trade data for 1985 were only available for the first four months and only on a settlements basis. According to these data, exports in terms of SDRs did not show any increase from the comparable 1984 period and were running somewhat below the rate envisaged under the program for 1985. For the rest of the year, however, the authorities expected an acceleration in the growth of export receipts. They indicated that, in particular, fish prices had been low during the first few months of the year, but had already started to rise and were expected to rise further in the second half of the year. They also expected iron ore exports to expand as a result of a recent increase in orders. During the first four months of the year, recorded imports--which exclude project-related imports directly financed from abroad--were higher than in the same period of 1984 and were running somewhat above the rate envisaged under the program for 1985. The main reason was that some imports had been postponed from late 1984 to early 1985. The authorities did not consider these developments representative of the year as a whole and projected that in 1985 recorded imports would be below the level assumed in the program. Project-related imports directly financed from abroad, which in 1984 had been much lower than previously estimated (see Table 3), 1/ were expected to stay well below the level assumed in the program.

The authorities expected that the surplus on the capital account would be smaller in 1985 than last year because the reduced investment level would be reflected in substantially lower loan disbursements, while scheduled repayments were expected to remain unchanged. The overall balance of payments deficit before debt relief was thus estimated at SDR 76.5 million. Together with the arrears on public and publicly guaranteed external debt and the arrears on the guaranteed

1/ The revised import estimate for 1984, from SDR 389.5 million in EBS/85/41 to SDR 294.7 million now, is mostly due to a revision in the estimate of project-related imports directly financed from abroad.

commercial credits, which all have to be eliminated in 1985, the Mauritanian authorities expected a financing gap of about SDR 190-195 million. This estimate assumed no reserve changes by deposit money banks or the Central Bank. As already noted, the Mauritanian authorities expected that this financing gap would soon be covered.

The Mauritanian authorities acknowledged that the weak balance of payments position required a flexible exchange rate policy. They explained that since the February 1985 devaluation, when all broken cross-rates had been eliminated, their exchange rate policy had aimed at a gradual reduction of the real effective exchange rate of the ouguiya. Between February and June 1985, the ouguiya was depreciated by about 2 percent in real effective terms. The Government reaffirmed its commitment to improve further the competitiveness of the external sector by keeping domestic price and cost increases low and by taking the appropriate exchange rate actions.

Mauritania continues to maintain discretionary controls on imports and on the sale of foreign exchange for invisibles, including travel expenses and remittances abroad by foreigners working in Mauritania. Substantial arrears on imports and on debt service payments were accumulated during 1982-84. The authorities confirmed their intention to eliminate all of the public and publicly guaranteed arrears before end-September 1985. As for arrears in respect of payments which are not subject to government guarantee, the authorities reaffirmed their intention to make foreign exchange available when domestic counterpart funds are provided by the importer or debtor.

IV. The Medium-Term Outlook

In cooperation with the staff of the World Bank, the Fund staff has prepared a medium-term balance of payments scenario covering the period 1985 to 1992 (Table 5). This scenario is based on a number of assumptions concerning developments in the Mauritanian economy, including the continuation of current adjustment policies and the successful implementation of the 1985-88 recovery plan, and on the assumptions for the world economy underlying the baseline scenario of the Fund's medium-term world economic outlook. It also assumes a return to more normal weather conditions.

In this scenario, growth of real GDP averages 2 1/2 to 3 percent over the forecast period, slightly higher than the projected population growth. Investment is expected to average 22 percent of GDP during 1986-92, that is, about the same as during 1984-85, with emphasis on increasing the efficiency of the existing plant and infrastructure. This implies a sharp decline from the average 34 percent of GDP during 1979-83. Domestic saving is expected to become positive and to cover

Table 5. Mauritania: Medium-Term Projections of Balance of Payments and Debt Service Payments, 1985-92

	1985	1986	1987	1988	1989	1990	1991	1992
				(In millions of SDRs)				
Trade balance, f.o.b.	10.6	31.9	42.1	64.9	88.7	107.2	123.3	146.6
Exports	316.8	346.8	371.9	431.6	464.6	499.3	548.0	603.9
Imports	-306.3	-314.8	-329.8	-366.7	-375.8	-392.1	-424.7	-457.3
Services (net)	-171.6	-172.8	-180.6	-187.4	-183.5	-188.9	-196.7	-211.4
Interest 1/	-50.3	-48.3	-48.4	-48.1	-49.2	-50.9	-52.0	-52.8
Other	-121.3	-124.5	-132.2	-139.3	-134.3	-138.0	-144.7	-158.6
Transfers	78.4	81.1	82.9	81.0	83.6	86.4	92.4	98.8
Private	-19.1	-18.2	-17.1	-16.1	-15.1	-14.2	-13.7	-13.3
Public	97.5	99.3	100.0	97.1	98.7	100.6	106.1	112.0
Current account balance								
Including public transfers	-82.6	-59.8	-55.6	-41.5	-11.2	4.7	19.0	34.0
Excluding public transfers	-180.1	-159.1	-155.6	-138.6	-109.9	-95.9	-87.1	-78.0
Nonmonetary capital (net)	6.1	-37.7	-10.8	-24.3	-35.8	-24.1	-15.0	-22.4
Disbursements	74.8	70.6	80.3	83.8	88.4	93.3	101.7	110.8
Principal repayments 1/	-71.2	-122.5	-105.8	-123.4	-122.1	-115.5	-115.0	-131.6
Direct investment	12.7	25.3	26.4	27.6	10.7	11.4	12.5	13.5
Other capital 2/	-10.2	-11.1	-11.7	-12.3	-12.8	-13.3	-14.2	-15.1
Overall balance before debt relief	-76.5	-97.5	-66.4	-65.8	-47.0	-19.4	4.0	11.6
Accumulation of arrears (+ indicates an increase)	-113.3 3/	-5.5 4/	--	--	--	--	--	--
Interest	-44.3	--	--	--	--	--	--	--
Principal	-69.0 3/	-5.5 4/	--	--	--	--	--	--
Reserve changes (- indicates an increase)	--	-2.8	-6.6	-11.5	-4.4	-5.6	-6.0	-5.5
Central Bank	--	-2.8	-6.6	-11.5	-4.4	-5.6	-6.0	-5.5
Of which: maturing liabilities	(--)	(-27.2)	(-23.2)	(-22.3)	(--)	(--)	(--)	(--)
net purchases from the Fund	(-2.6)	(-7.3)	(-4.9)	(-3.8)	(-6.8)	(-4.5)	(-0.3)	(--)
Deposit money banks	--	...	...	...	...	...	...	...
External debt relief and exceptional assistance	198.3 5/	27.8	...	...	...	...	...	...
Financing gap (surplus -)	-5.8	112.5	101.1	103.4	58.2	29.5	2.3	-6.1
				(In percent of GDP)				
Current account balance								
Including official transfers	-12.3	-8.8	-7.3	-5.2	-1.3	0.5	1.9	3.3
Excluding official transfers	-26.9	-23.3	-20.6	-17.3	-13.0	-10.8	-9.0	-7.3
				(In percent of exports of goods and services)				
Total debt service	36.0	51.3	42.2	40.0	33.5	30.0	26.8	26.9
Interest and charges	13.5	11.9	11.2	9.7	9.3	8.9	8.3	7.7
Principal and repurchases	22.5	39.4	31.0	30.3	24.3	21.0	18.5	19.2

Sources: Data provided by the Mauritanian authorities; and staff estimates.

1/ Including debt service on financing of the gap.
2/ Including private and short-term capital and errors and omissions.
3/ Including SDR 2.8 million in arrears on guaranteed commercial credit and SDR 5.5 million in arrears on unguaranteed commercial credit.
4/ Unguaranteed commercial arrears.
5/ Including special assistance from Saudi Arabia (SDR 30.5 million).

about 60 percent of investment expenditures by the late 1980s. This favorable development would reflect both a reduction in the share of private consumption in GDP and an increasing surplus in the Government's current operations. This will require persistent restraint in fiscal and monetary policy and a competitive exchange rate.

The assumptions and policies mentioned above are expected to result in sizable current account surpluses (including public transfers) by the early 1990s. This is due to a gradual increase in iron ore exports and substantial increases in fish exports, while on average imports are expected to increase by only 1 percent a year in real terms. Fish exports are expected to become Mauritania's major export by 1986, replacing iron ore. The net contribution of the fishing sector to the current account will increase even more than recorded fish exports, because payments for imported services and profit remittances to foreign partners are projected to decrease in real terms as the national fleet and onshore facilities are developed. The copper project, which is scheduled for completion in 1987, is expected to contribute only slightly to the current account, as payments for imported inputs are projected to offset a large part of export receipts. The projected sluggish import demand will stem from the February 1985 devaluation and the subsequent adoption of a flexible exchange rate policy, the reduced investment level, and increased agricultural production.

In contrast to the improving current account, the capital account is expected to become strongly negative starting in 1986 because of a dramatic increase in scheduled debt repayments coming shortly after a decrease in foreign loan disbursements. The result is that the overall deficit (before debt relief) and the financing gap will decline quite slowly, and will be eliminated only in the early 1990s. Nevertheless, the debt situation would improve markedly during the forecast period; the total debt service ratio would decline from 36 percent of exports of goods and nonfactor services in 1985 to 27 percent in the early 1990s (see Table 5). During 1986-88, the financing gap is projected to be equivalent to two thirds of total debt service due, which would roughly equal that part of the debt service which is eligible for rescheduling. After 1988, the financing gap declines rapidly below 30 percent of total debt service due.

The current medium-term balance of payments projection differs from that for 1986-90 contained in the program paper, EBS/85/41, in three main respects. First, export prices of iron ore in terms of SDRs are now projected to increase by about 4 percent a year, versus 7 percent a year in the previous scenario. Second, the new scenario assumes lower public investment and a higher share of foreign grants in the financing of investment than earlier expected, in line with the assumptions of the 1985-88 recovery plan. And third, the new scenario assumes less favorable terms of financing for the balance of payments

gap. In the program paper, a five-year grace period and sixteen-year maturity were assumed, while the new scenario assumes a six-year grace period and thirteen-year maturity. The net effect of these revisions is a resorption of the financing gap that is somewhat slower than previously anticipated.

The scenario presented above is currently considered the most likely outcome if the assumptions are realized. If the Mauritanian adjustment policy were not continued, the outcome would be considerably worse. For example, a 2 percent higher annual rate of increase of food and consumer goods imports above the assumed rate would widen the balance of payments gap by almost SDR 10 million annually around 1990. The outcome would also be worse if iron ore prices were to weaken significantly; a 2 percent lower annual rate of increase in iron ore prices would widen the balance of payments gap by about SDR 20 million annually around 1990.

V. The Financial Program for the Second Half of 1985

The Government, aware that the next several years will be extremely difficult, is determined to continue the adjustment envisaged in the memorandum on the economic and financial policy attached to its letter of intent of January 25, 1985. In particular, during the second half of 1985, it will continue to adjust the exchange rate and administered domestic prices in accordance with the principles set forth in that memorandum. Those administered prices which had not been increased to reflect the effects of the February devaluation, and for which the economic agents concerned had filed documented requests for adjustments, were increased in August. Also in August, the Government introduced a mechanism that will result in the automatic adjustment of all administered prices in line with the adjustment of the exchange rate within four weeks. To speed up the gradual liberalization of pricing policies, the authorities will complete by end-October 1985 their study of the changes that should be made in the present marketing and pricing systems in order to liberalize them. The specific measures envisaged as a result of this study will be examined by the staff at the time of the second review.

In the budgetary area, the Government will intensify its efforts to increase tax yields. It will also conduct a coordinated program of recruitment and employment terminations during the period from August to November 1985. During this period, the Government will recruit up to 800 school graduates educated abroad or in the national training schools. At the same time, however, the Government will take measures to ensure that recruitment does not exceed employment terminations by more than 100 by the end of September and that they are equal by the end of November. These measures should ensure that Mauritania attains the budgetary targets for 1985 set forth in the memorandum of January 25, 1985.

In conformity with the Government's budgetary targets for 1985, the financial program for the second half of 1985 targets that net bank credit to the Government, which was equal to UM 5,016 million at end-December 1984 and UM 4,914 million at end-June 1985, will not exceed UM 5,016 million at end-September 1985 and end-December 1985 (Table 6). The end-December ceiling will be automatically revised downward by the amount of any net foreign financing, including assistance to the Government resulting either from the rescheduling of its external debt or from exceptional financial assistance, exceeding that necessary to finance the Treasury deficit (UM 403 million) set as a target in the program.

Overall bank credit, which equaled UM 19,762 million at end-December 1984 and UM 19,854 million at end-June 1985, will not exceed UM 20,650 million at end-September and UM 20,850 million at end-December. The end-December ceiling will be revised downward automatically in an amount equal to the adjustment in the ceiling for net bank credit to the Government referred to above. These ceilings are consistent with an increase in total bank credit of less than 6 percent for 1985 as a whole and an increase in credit to the economy of less than 8 percent. The ceilings are somewhat higher than the indicative targets of UM 20,450 million for end-September and UM 20,660 million for end-December set out in the memorandum of January 25, 1985. The change was motivated by two main factors: (i) the final figure on outstanding domestic credit at end-1984 is UM 120 million higher than the figure projected when the program was drawn up in early 1985; and (ii) the increase in credit attributable to the capitalization of interest on nonperforming loans by commercial banks is substantially higher than initially envisaged. With these credit ceilings, the expansion of money and quasi-money would reach about 14 percent for 1985 as a whole, in line with the expansion of nominal GDP.

It is expected that the Fund staff will conduct discussions for the second review under the program in early December 1985, and that the review will be completed in February 1986.

VI. Staff Appraisal

Over the past two years, the Government of Mauritania has undertaken a major adjustment effort. In particular, it has taken a number of decisive supply-side measures, including a depreciation of the real exchange rate, an increase in prices of cereals at the producer and consumer levels, and a rise in interest rates to a level consistent with the underlying inflation rate. It has also cut domestic demand through a sharp tightening of financial policies. Largely as a result of these measures, the external current account deficit (including public transfers) is expected to decline from about 28 percent of GDP in 1983 to 12 percent of GDP in 1985. The 1985 gap-fill exercise is expected to be completed shortly, and the implementation of the Fund-supported financial program for 1985 remains on track.

Table 6. Mauritania: Quantitative Performance Criteria, 1985

(End of period)

	1984		1985							
	December		March		June		September		December	
	Program	Actual	Ceiling	Actual	Ceiling	Actual	Initial limits	Ceiling	Initial limits	Ceiling
					(In millions of ouguiyas)					
Net domestic credit 1/	19,642	19,762	19,850	19,319	20,050	19,854	20,450 2/	20,650 3/	20,660 2/	20,850 3/
Net credit to Government	5,142	5,016	5,142	4,785	5,142	4,914	5,152 2/	5,016 3/	5,142 2/	5,016 3/4/
Domestic arrears of the Government	742.0	700.0	556.5	26.0	371.1	--	185.5	185.5 5/	--	--
					(In millions of SDRs)					
New nonconcessional foreign borrowing contracted or guaranteed by the Government with 0-12 years' maturity 6/	...	--	--	--	--	--	--	--	--	--
External arrears on medium- and long-term public and publicly guaranteed debt	93.3	104.8	93.3	...	93.3	...	--	--	--	--
External arrears on guaranteed commercial credit	3.1	3.1	3.1	3.1	--	2.8 7/	--	--	--	--

Sources: Data provided by the Mauritanian authorities; and staff estimates.

1/ Precludes any reclassification of credit to other monetary items during the program period.
2/ Tentative credit limits indicated in EBS/85/41.
3/ Credit ceilings set during the first program review.
4/ Under the program the ceiling on net credit to the Government will be adjusted downward by an amount equal to the financing surplus.
5/ Initial ceiling; no further accumulation of domestic arrears is allowed during the program period.
6/ Excluding debt rescheduling.
7/ These guaranteed commercial arrears were eliminated in July 1985.

The Government is aware that misallocation of resources and poor management of projects were largely responsible for the low yield from investment and the contraction of the production base. To generate a higher yield on investment, the Government is scaling down and rationalizing the public investment program, orienting it toward the support and development of directly productive activities. The 1985 public investment program appropriately emphasizes the development of the rural sector and the rehabilitation of the existing capital stock. The Economic and Financial Recovery Plan for 1985-88, which was recently prepared in cooperation with the World Bank, envisages a continuation of the new policy, with public investment limited to 20 percent of GDP and concentrated on projects that will enhance production and improve the balance of payments. This recovery plan also stresses the role of private investment, including private foreign investment. The staff welcomes this new investment policy which the Mauritanian authorities rightly regard as the cornerstone of their adjustment strategy.

To foster an expansion of the production base, the new investment policy must be supported by the right price signals. As the three sectors that have appropriately been selected to lead the expansion--namely fishing, agriculture, and mining--are producing internationally traded goods, it will be particularly important to maintain a flexible exchange rate policy. The substantial depreciation of the ouguiya in real effective terms during January-July 1985 has already gone a long way in improving price incentives in those sectors, but, in the staff's view, further improvements are needed. In addition, the staff considers that domestic pricing and marketing policies should be liberalized further. It is of course true that the private sector is quite limited and that an abrupt liberalization could be misused by private monopolies. However, the weakness of the private sector is itself the result of many years of price controls and marketing monopolies for public enterprises. This vicious circle should be broken by a clear indication of the Government's commitment to a policy of gradual but significant liberalization and by its steady implementation.

Apart from price liberalization, the expansion of the production base will largely depend on the success of the current program in rehabilitating public enterprises. For example, the development of irrigation is possible only if the cost of setting up and maintaining the irrigated areas is cut substantially. In part, this should be achieved through an increase in the efficiency of SONADER, the public enterprise in charge of rural development. Similarly, despite recent progress, the output per employee of SNIM, the iron ore company, is still about 40 percent lower than in the late 1960s, largely because of overstaffing. In the fishing sector, it will be difficult to develop onshore processing activities as long as the cost of water and electricity in Nouadhibou remains three times higher than in the Canary Islands

or in Senegal, mainly because of the low productivity of SONELEC, the public enterprise in charge of electricity and water supply. In all these instances, exchange rate depreciation cannot be viewed as an alternative to the needed productivity improvement.

Another key condition for the success of the adjustment effort is that a significant part of the expansion of the production base be financed by domestic savings. Through at least the end of the 1980s, much of these savings will have to come from public enterprises and the Government. Among public enterprises, SNIM will have a preponderant role to play. Currently, it is envisaged that SNIM will finance nearly 42 percent of its 1986-88 investment through the use of internal resources. This obviously requires a further increase in its profitability through productivity increases. For the Government, the challenge is to generate a substantial surplus on Treasury current operations and to cut the large deficit in the consolidated budget. To achieve this objective, the Government has implemented a number of measures to raise tax revenues and cut the growth of government current expenditures. For 1985, the aim is to generate a Treasury current surplus of 0.9 percent of GDP that would cover about 7 percent of government investment expenditure. The staff views this aim as a minimum requirement. Thus, it welcomes the strong determination of the authorities to strengthen tax collection in order to make up the shortfalls in tax revenue experienced during the first half of 1985. Over the next several years, this surplus will have to grow substantially. As the tax effort is already fairly large, this will require a continuation of tight controls on the growth of government current expenditures, particularly with respect to military expenditures and the wage bill for the civil service. In this regard, the Government's recent decision to discontinue its policy of automatic recruitment of graduates from national professional training schools is welcomed.

In the recent period of major adjustment, the authorities have maintained a cautious monetary policy, with a decline in net credit to the Government and a small expansion of credit to the rest of the economy. This cautious monetary policy, supported by a strict incomes policy in the public enterprises and in the administration, has prevented the exchange rate depreciation from giving rise to an inflationary process. With inflation remaining moderate, current interest rates for deposits and loans seem adequate. The weak point in the monetary area remains the precarious financial situation of the commercial banks. As soon as the study of the banking sector currently in progress is completed, which should be in October 1985, the authorities should take appropriate measures to rehabilitate the commercial banks, strengthen their risk assessment procedures, and ensure that a system of inspection is put in place in order to avoid a recurrence of the problem.

There have been no changes in the exchange and trade system since the last Article IV consultation. As part of the program, the authorities are committed to eliminate by end-September arrears that have been accumulated on public and publicly guaranteed debt. The staff therefore recommends the approval of the restrictions pertaining to such arrears until September 1985. As for arrears in respect of payments which are not subject to government guarantees, the authorities reaffirm their intention to make foreign exchange available when domestic counterpart funds are provided by importers or debtors. In these circumstances, any delays in making of payments would not constitute an exchange restriction subject to approval by the Fund.

In its medium-term scenario, the staff projects that Mauritania will re-establish a viable balance of payments by the early 1990s. However, the staff would stress that this projection is highly conditional on a number of favorable assumptions; the most crucial is that Mauritania will be successful in boosting the foreign exchange yield of new investment, while cutting its foreign exchange cost. In the view of the staff, this will require not only a careful allocation of resources and a good management of projects, but also a strict control of the size of the public investment program, in particular, over the next two to three years. A program equivalent to 20 percent of GDP, as envisaged in the recovery plan, is probably the maximum that is consistent with the current limited scope for viable projects and the scarcity of domestic savings and foreign grants.

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

VII. Proposed Decisions

1985 Consultation

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

2. Mauritania maintains a restriction on payments and transfers for current international transactions giving rise to external payments arrears, which is subject to approval under Article VIII, Section 2 (a). The Fund welcomes the elimination of the multiple currency practice arising from broken cross-rates and urges Mauritania to eliminate the exchange restiction giving rise to external payments arrears.

Review Under the Stand-by Arrangement

1. Mauritania has consulted with the Fund in accordance with paragraph 4(e) of the stand-by arrangement for Mauritania (EBS/85/41, Supplement 2) and paragraph 3 of the letter of the Governor of the Central Bank of Mauritania dated January 25, 1985, annexed thereto, in order to review policies and establish performance criteria for the second semester of 1985.

2. The letter dated September 17, 1985 from the Governor of the Central Bank of Mauritania shall be attached to the stand-by arrangement for Mauritania, and the letter dated January 25, 1985 shall be read as modified and supplemented by the letter of September 17, 1985.

3. Mauritania will not make purchases under the arrangement that would increase the Fund's holdings of Mauritania's currency in the credit tranches beyond 25 percent of quota

(a) during any period in which the data at the end of the preceding period indicate that:

(i) the limit on total net domestic credit of the banking system specified in paragraph 8 of the letter of September 17, 1985, or

(ii) the limit on net bank credit to the Treasury specified in paragraph 7 of the same letter

has not been observed;

(b) after February 15, 1986, until the second review under the arrangement contemplated in paragraph 11 of the letter of September 17, 1985 has been completed.

4. In view of the understandings reached with Mauritania in the context of this review, the Fund decides that the review is completed and that Mauritania may proceed to make purchases under the arrangement.

Mauritania: Selected Economic and Financial Indicators, 1981-85

	1981	1982	1983	1984 Estimates Previous 1/	1984 Estimates Revised	1985 Program 1/	1985 Projection
	(Annual percentage changes, unless otherwise specified)						
National income and prices							
GDP at constant prices	3.7	-2.2	6.0	-5.0	-0.5	3.0	2.5
GDP deflator	7.0	9.9	4.0	9.0	11.2	12.0	11.0
Consumer price index 2/	11.5	8.4	4.9	9.0	8.0	12.0	12.0
External sector							
Exports, f.o.b. (in SDRs)	52.3	-5.7	36.3 3/	-3.2	-2.8	13.7	10.5
Imports, f.o.b. (in SDRs)	33.1	17.1	-9.1	10.1	-16.7	11.7	3.9
Export volume	36.2	-8.2	43.0	-7.7	-6.2	5.5	1.6
Import volume	22.5	16.1	-8.0	-1.8	-18.2	-11.3	--
Terms of trade 4/	9.9	1.9	-2.7	-0.6	1.9	1.7	1.6
Effective exchange rate (depreciation -)	11.7	6.6	4.3	-8.9	-6.3	...	...
Consolidated government operations							
Revenue	-29.5	8.1	23.9	16.8	15.3	19.3	20.9
Revenue and grants	15.9	1.1	12.5	30.7	22.6	24.1	20.3
Total expenditure	8.6	22.0	11.4	19.3	9.8	10.6	8.8
Money and credit							
Domestic credit	15.8	21.1	10.0	8.6	9.3	5.2	5.5
Credit to the Government	(27.5)	(13.1)	(30.6)	(--)	(-2.4)	(--)	(--)
Credit to the economy	(12.5)	(23.9)	(1.5)	(12.0)	(13.9)	(7.0)	7.4
Money and quasi-money	33.2	-2.0	9.1	9.1	9.0	9.2	14.3
Velocity (GDP relative to M2)	4.1	4.2	4.3	4.1	4.2	4.3	4.2
Interest rate 5/	9.0	9.0	9.0	9.0	9.0	11.0	11.0
	(In percent of GDP)						
Consolidated government deficit 6/							
Excluding grants	16.5	23.4	21.4	24.5	20.9	21.8	17.7
Including grants	4.5	11.5	11.2	9.1	7.8	4.2	4.1
Change in payments arrears (increase +)	1.2	1.3	1.0	1.4	1.4	-19.9	-15.7
Consolidated government deficit (cash basis)	3.4	10.2	10.2	7.7	6.4	17.1	19.8
Foreign financing (net)	10.6	13.9	10.0	7.4	7.2	-2.1	-2.0
Domestic financing (net)	-7.2	-3.7	0.2	0.3	-0.8	--	--
External debt relief and exceptional assistance	--	--	--	--	--	--	21.8
Financing gap (surplus -)	--	--	--	--	--	19.2	-0.1
Budgetary deficit 7/	-1.0	3.0	4.7	1.0	1.8	0.9	0.8
Gross domestic investment	41.9	47.1	17.9	36.9	22.4	15.2	21.4
Gross domestic savings	12.4	3.4	-11.2	-0.6	-0.7	2.5	4.7
Resource gap	-29.4	-43.7	-29.1	-37.5	-23.1	-12.7	-16.7
Current account deficit							
Excluding official transfers	34.7	51.3	38.3	48.9	32.5	21.6	16.9
Including official transfers	21.2	39.9	26.2	33.5	19.6	14.1	12.3
External debt 8/ (outstanding)	125.0	153.0	164.2	202.6	175.1	142.5	206.1
Debt service ratio 9/	31.5	29.7	30.3	37.8	38.4	36.5	36.0
	(In millions of SDRs, unless otherwise specified)						
Overall balance of payments							
Before debt relief	-23.5	-108.1	-82.9	-101.2	-106.4	-71.5	-76.5
After debt relief	30.7	-86.3	-56.6	-72.0	-77.0	...	5.8
Gross official reserves (months of imports of goods and nonfactor services)	2.6	2.7	2.7	1.5	2.0	3.0	2.1
Net foreign assets 10/	-12.9	-73.9	-110.5	-145.5	-142.9	-145.5	-137.0
External payments arrears 11/ (outstanding)	20.5	36.5	55.4	93.5	104.8	--	--

Sources: Data provided by the Mauritanian authorities; and staff estimates.

1/ As indicated in EBS/85/141.
2/ For low-income group with Mauritanian consumption pattern.
3/ The rapid increase in exports is due to the fishing sector.
4/ In SDR terms.
5/ Annual maximum deposit rate.
6/ On a commitment basis, including central government operations, development expenditures financed directly through external aid, and interest charges to be refinanced or rescheduled.
7/ Deficit on Treasury operations, on a commitment basis.
8/ Inclusive of Fund resources and central bank deposits.
9/ As a percentage of exports of goods and services.
10/ Of the banking system.
11/ On public and publicly guaranteed medium- and long-term debt.

Mauritania: Summary of Principal Policy Measures of the 1985 Program and Their Implementation

A. External sector policies	
a. A 16 percent devaluation of the ouguiya followed by a gradual depreciation in real terms.	Implementation as envisaged.
b. Elimination of broken cross-rates.	Implemented.
c. Elimination of outstanding arrears on public and publicly guaranteed external debt, with no further accumulation.	Not yet implemented; in accordance with agreed timetable, this action is to be taken by end-September 1985.
d. Elimination of guaranteed commercial arrears, with no further accumulation.	Implemented.
e. No new nonconcessional loans in the 0-12 year maturity range (excluding debt rescheduling).	Implementation as envisaged.
B. Fiscal policy	
The fiscal deficit on a commitment basis (including grants and before debt relief) will be reduced from 9.1 percent of GDP in 1984 to 4.2 percent of GDP in 1985; excluding grants, from 24.5 percent of GDP to 21.8 percent. The level of public employment is frozen.	The authorities have reaffirmed their commitment in this regard.
C. Monetary policy	
a. An increase in interest rates of 2 percentage points.	Implemented.
b. A strengthening of central bank monitoring of commercial bank activities.	Implementation as envisaged.
c. Rehabilitation and strengthening of the banking sector.	Not yet implemented. Completion of the needed study was delayed. It should now become available in November 1985.
D. Pricing and marketing policies	
a. An increase in official prices for consumer goods, public utilities, petroleum products, and agricultural producer prices, to reflect at least the full pass-through effects of the exchange rate adjustment on prices.	Implemented with some delays.
b. Gradual liberalization of pricing and marketing policies.	Not yet implemented. Completion of the needed study was delayed. It should now become available by end-October 1985.
E. Public enterprises	
a. Rehabilitation of five key public enterprises.	Implementation as envisaged.
b. Prepare for the rehabilitation of other public enterprises.	Implementation as envisaged.
c. Set a timetable for settlement of the interlocking debts of SONELEC, OPT, EMN and the Government.	Implemented.
F. Public investment program	
a. The public investment program for 1985 is limited to US$183 million, with a maximum implementation rate of 70 percent.	Implementation as envisaged.
b. Preparation, in consultation with the World Bank, of an investment program for the period 1986-88.	Implementation as envisaged.

Nouakchott, September 17, 1985

Dear Mr. de Larosière:

Under the stand-by arrangement approved by the International Monetary Fund on April 12, 1985, it was stipulated that the Government of the Islamic Republic of Mauritania would review with the Fund the outcome of the exercise to bridge the financing gap and the progress made under the program during the first half of 1985. The Government would also reach understandings with the Fund on the economic and financial policies, including performance criteria, for the second half of the year. Discussions with Fund staff for this review took place in conjunction with the Article IV consultation discussions in Nouakchott in July 1985 and at Fund headquarters in August 1985.

1. The Government implemented all the key measures envisaged under the program for the first half of 1985. Specifically, the exchange rate was devalued by 16 percent on February 14 and subsequently adjusted in accordance with the terms of the arrangement, and agricultural prices were increased both at the producer level and at the marketing stage. Most official prices for consumer goods and petroleum products were increased to reflect the devaluation. In order to improve Mauritania's resource allocation and to strengthen the role played by Mauritanian banks as financial intermediaries, interest rates for deposits and loans were also increased, taking into account the rate of inflation, corrected for the temporary surge resulting from the February devaluation. These measures were supported by the introduction of a restrictive policy as regards the Central Government's budget and the amount of credit, as well as by an economic and financial recovery policy based on a reform of the key public enterprises and the banking system and the implementation of a public investment program prepared in cooperation with the World Bank, with an overall implementation ratio of 70 percent.

2. All the quantitative performance criteria for end-March and end-June were observed, with the exception of the criterion pertaining to external payments arrears on guaranteed commercial loans for end-June, which the Government requests be waived. Negotiations on the SDR 3.1 million in arrears on guaranteed commercial loans that were identified when the program was drawn up have taken somewhat longer than anticipated. Arrears of about SDR 2.8 million were eliminated in early July through rescheduling arrangements. The remaining amount represents a loan now in litigation in the Spanish courts. A comprehensive survey undertaken by the authorities in April 1985 did not uncover any other arrears on guaranteed commercial credit, or on nonguaranteed commercial credit for which the domestic counterpart had been paid. An inventory of domestic arrears, completed in April 1985, showed a total of UM 751 million as of end-1984, somewhat higher than the earlier estimate of UM 742 million. During the first months

of 1985, all domestic arrears were liquidated, ahead of the schedule stipulated in the program. The Government has undertaken, as a performance criterion, not to accumulate any new domestic arrears during the program period.

3. Thanks to the efforts made under the program, we have begun to reduce the economic and financial imbalances our country has experienced for many years. In the fiscal area, budgetary revenue for the first six months of 1985 was significantly higher than during the corresponding period of 1984, even though it fell somewhat short of the program target. Budgetary expenditure developments have been in line with program projections. Judging from the data available to us, the balance of payments on current account has continued to improve over the first five months of 1985. Recovery programs for the key public enterprises have been implemented during the same period, and the first steps have been taken toward the financial rehabilitation of these enterprises, by improving their productivity and substantially increasing their rates.

4. As regards the financing gaps in the Central Government's budget and the balance of payments, the recent meeting of the Paris Club and discussions with other creditor countries have resulted in substantial assistance in the form of debt rescheduling and exceptional external assistance on concessional terms. While it is still too early to quantify the amount of this assistance precisely, it now appears likely that budgetary assistance will at least cover the financing gap corresponding to the budgetary targets set forth in the program. These targets are intended to reduce the 1985 budget deficit on Treasury operations to UM 403 million (0.8 percent of GDP) and the deficit of the consolidated budget on a commitment basis, including grants and before debt relief, to UM 2,176 million (4.2 percent of GDP). Similarly, it is now likely that balance of payments assistance will at least equal the estimated financing gap corresponding to the program targets for the overall balance of payments deficit before exceptional financing.

5. Encouraged by the results obtained so far, and taking into account the rescheduling of the external debt and other exceptional external assistance expected, the Government is determined to continue the task of adjustment envisaged in the memorandum on the economic and financial policies attached to my letter of January 25, 1985. In particular, it is resolved to continue the adjustment of the exchange rate and prices in accordance with the policies set forth in that memorandum. Those official prices which had not yet been increased to reflect the effects of the February devaluation and for which the economic units concerned had filed documented requests for adjustments were increased in August 1985. Also in August, the Government introduced a mechanism that will result in the automatic adjustment of all official prices in line with the adjustment of the exchange rate within a maximum time lag of four weeks. Priority will also be accorded to reviewing the floor price for paddy paid by the CSA, with a view to determining whether it is sufficiently high to constitute an incentive for domestic production.

Similarly, discussions now under way with the World Bank on the adjustment of the SONELEC rate schedule, or other measures necessary for the financial recovery of that agency, will be completed by October 1985. In the budgetary area, the Government will be intensifying its efforts to increase tax yields. It also will prepare a joint presentation of current and investment operations, as a first step toward a consolidated government budget, before the second program review with a view to improving information on the Central Government's financial operations. The Government has requested assistance from the Fund in this regard.

6. Through July 1985, the Government has maintained the freeze on civil service staffing levels referred to in my letter of January 25, 1985, by limiting new recruitment to the few openings resulting from retirements, resignations, and deaths. However, during the remainder of 1985, the Government will recruit up to 800 school graduates educated abroad or in the national professional training schools. Up to 500 of these graduates will be recruited in August and September, and the rest in October and November. There will be no recruitment in December. The Government had guaranteed civil service employment to these graduates when they began their courses of study, and their recruitment is necessary in order to achieve an improvement in the professionalism of the administration. Approximately 85 percent of these graduates are teachers or medical personnel. The Government, aware of the heavy burden occasioned by the current automatic recruitment system and of the surpluses that exist in certain employee categories, is preparing measures that will enable it to offset this recruitment by an equal number of employment terminations. Specifically, the Government will take measures to ensure that the number of employment terminations does not fall short of the number of new recruitments by more than 100 by the end of September 1985 and equals the number of new recruitments by the end of November 1985. These measures include better control of attendance, early retirement, a reduction in the number of technical assistants paid out of the Mauritanian budget, removal from the budget payroll of individuals already employed and paid by parastatals, and voluntary departures resulting from a freeing of recent recruits from their contractual obligations to work for the Government. The Government is resolved to take any supplementary measures which may prove necessary to that effect. The actual number of new recruits and employment terminations will be communicated to the Fund during the first week of October 1985 for the August-September period, and during the first week of December 1985 for the October-November period. In addition, the Government will discontinue its automatic recruitment policy in order to avoid rapid growth of civil service employment in future years.

7. In conformity with the Government's budgetary targets for 1985, and as a performance criterion, net bank credit to the Treasury, equal to UM 5,016 million at end-December 1984 and UM 4,914 million at end-June 1985, will not exceed UM 5,016 million at end-September 1985 and end-December 1985. The end-December ceiling will be automatically

revised downward by the amount of net assistance to the Government resulting either from the rescheduling of its external debt or from exceptional financial assistance in amounts exceeding those necessary to finance the Treasury deficit level set as a target (UM 403 million), taking into account the elimination of arrears at end-1984 (currently estimated at UM 8,414 million), the amortization payable by the Central Government in 1985 (currently estimated at UM 4,316 million), and drawings on financing (currently estimated at UM 1,476 million).

8. Overall bank credit, which equaled UM 19,762 million at end-December 1984 and UM 19,854 million at end-June 1985, will not exceed UM 20,650 million at end-September 1985 and UM 20,850 million at end-December 1985. The end-December ceiling will be revised downward automatically in an amount equal to the adjustment in the ceiling for net bank credit to the Treasury referred to in paragraph 7. These ceilings for overall bank credit constitute performance criteria and are consistent with an increase in total bank credit of less than 6 percent for 1985 as a whole and an increase in credit to the economy of less than 8 percent.

9. The Government of the Islamic Republic of Mauritania is aware of the delays that have occurred as regards the rehabilitation and strengthening of the banking sector and the gradual liberalization of price policies. A financing problem has delayed completion of the study on the banking system. However, this study, now largely financed by the World Bank, will be completed in October 1985. The second review under the arrangement will examine its conclusions and draw up a timetable for the implementation of the recommendations in agreement with the authorities. Similarly, the staff of the Ministry of Finance and Commerce undertakes to complete by end-October 1985 the study aimed at identifying the changes that should be made in the present marketing and pricing systems with a view to liberalize them. The specific measures envisaged on the basis of this study will also be examined at the time of the second review.

10. The Government remains firmly resolved to spare no effort to accelerate the achievement of the program now under way for the rehabilitation of the public enterprise sector. In this regard, it undertakes to begin, by October 1, 1985, the study on the legal framework for relations with these public enterprises so as to be able to negotiate contractual agreements with them in the shortest possible time. In addition, the audit of public enterprises will be initated within two months following approval of the IDA credit, with priority given to the OPT. The Government is also resolved, within the context of the 1985-88 financial recovery program, to confine itself to viable projects that will contribute directly to the creation of permanent jobs, to an increase in domestic production, and to the promotion and diversification of exports or the substitution of domestic for imported goods.

In this framework, the Government will give special attention to projects that can be carried out in part by using Mauritanian resources, rather than projects requiring large external borrowing.

11. It is expected that the Fund staff will conduct discussions for the second review under the arrangement in early December 1985, and that the review will be completed in February 1986.

12. This letter supplements my letter of January 25, 1985.

Very truly yours,

Dieng Boubou Farba
Governor
Central Bank of Mauritania

MAURITANIA - Relations with the Fund

(As of August 31, 1985, amounts in SDRs unless otherwise indicated)

I. Membership Status

(a) Date of membership: September 10, 1963
(b) Status: Article XIV

(A) Financial Relations

II. General Department (General Resources Account)

(a) Quota: 33.9 million
(b) Total Fund currency holdings: 60.42 million (177.70 percent of quota)
(c) Fund credit: 26.33 million (77.67 percent of quota)
(d) Reserve tranche position: None
(e) Current operation budget (maximum use of currency): None
(f) Lending to the Fund: None.

III. Current Stand-By and Special Facilities

	Type	Date of Approval	Duration	Amount	Utilization
(a)	Current arrangement:				
	SBA	April 12, 1985	12 months	12.0 million	4.8 million
(b)	Previous arrangements:				
	SBA	July 23, 1980	11 months 1/	29.7 million	8.9 million
	SBA	June 1, 1981	10 months	25.8 million	25.8 million
(c)	Special facilities:				
	CFF	December 1979		10.5 million	

IV. SDR Department

(a) Net cumulative allocation: 9.72 million
(b) Holdings: 492 (0.01 percent)
(c) Current designation plan (amount of maximum designation): None

1/ Arrangement became inoperative and was replaced by a new stand-by arrangement in June 1981.

MAURITANIA - Relations with the Fund (continued)

V. Administered Accounts

(a)	Trust Fund loan:	
	(i) Disbursed:	12.70 million
	(ii) Outstanding:	9.21 million
(b)	SFF Subsidy Account:	1.92 million

VI. Overdue Obligations to the Fund: None

(B) Nonfinancial Relations

VII. Exchange Rate Arrangement

Since January 22, 1974, the exchange rate of the ouguiya has been determined on the basis of a basket of currencies.

VIII. Last Article IV Consultation

The staff report for the 1984 Article IV consultation (SM/84/257) and the report on recent economic developments (SM/84/262) were considered by the Executive Board on December 10, 1984.

1. The Fund takes this decision relating to Mauritania's exchange measures subject to Article VIII, Sections 2 and 3, in concluding the 1984 Article XIV consultation with Mauritania, in light of the 1984 Article IV consultation with Mauritania conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. Mauritania's exchange system involves broken cross-rates and external payments arrears as described in SM/84/257. The Fund urges the authorities to adopt effective policies that will enable them to eliminate the broken cross-rates and external payments arrears and to liberalize the exchange system as soon as possible.

IX. Technical Assistance (since 1980)

(a) CBD

Technical assistance mission to study the banking system: April 1-11, 1980.

Bank supervision advisor: February 1981-June 1983 and September 1983-October 1984

MAURITANIA - Fund Relations (concluded)

IX. Technical Assistance (concluded)

Foreign exchange advisor: November 1980-May 1983 and May 1983-June 1985

Research department advisor: February 1981-June 1985

External debt consultant: May-October 1983

(b) Fiscal

Technical assistance mission on tax administration and policy, budget administration, and expenditure policies: September 20-October 18, 1983

Tax advisor: July 1984-August 1985

X. Resident Representative: None

MAURITANIA - Financial Relations with the World Bank Group

(As of March 31, 1985)

1. Date of membership, IBRD/IDA: September 10, 1963

2. Capital subscription, IBRD: SDR 10 million
   IDA: US$577 thousand

3. Status of disbursements: Amount (less cancellations) (In millions of U.S. dollars)

	Committed		Disbursed	
	IBRD	IDA	IBRD	IDA
One loan and ten credits fully disbursed	66.0	39.8	66.0	39.8
Agriculture, livestock and rural development		30.6		14.0
Transportation		4.0		1.2
Education		5.7		2.9
Industry	60.0	13.3	60.0	7.4
Energy		3.0		1.6
Parapublic		16.4		
Technical assistance		4.6		1.7
Total	126.0	117.4	126.0	68.6
Repayments	69.0	2.1	69.0	2.1
Debt Outstanding	57.0	115.3	57.0	66.5

4. IFC: There are no IFC investments in Mauritania.

5. Status of Bank Group dialogue and operations

To date, the Bank Group has had 22 operations in Mauritania for a total of US$239.9 million. Of these, two are Bank loans for mining operations (US$66 million for MIFERMA in 1960, and US$60 million for SNIM in 1979 for the Guelbs Iron Ore Project). The other 20 are IDA credits totalling US$114.2 million. In 1985, IFC has financed an edible oil refinery. At present, the Bank Group's share in Mauritania's external capital assistance amounts to about 8.0 percent.

After a comprehensive review of the public enterprise sector financed under the first Technical Assistance Project, assistance was also provided enterprises in preparing a medium-term rehabilitation program for the public enterprise sector. This program includes measures to increase the efficiency of existing enterprises through selective rehabilitation, privatization and liquidation and outlines rehabilitation programs for several of these enterprises, including pricing policies, personnel adjustments, streamlining of management and appropriate maintenance of equipment. In support of this program, a Public Enterprise Technical Assistance and Rehabilitation Project is scheduled to be presented to the Board of Executive Directors during FY 1985.

In order to address Mauritania's severe balance of payments problems, tight fiscal situation, and inability to service its public debt, the Bank Group, in close cooperation with the IMF, is helping the Government to prepare a Rehabilitation Program (1985-88) to be presented to a Consultative Group meeting scheduled for November 1985.

Assistance to the education sector is being provided under the Second Education Project (FY 1982) which aims at expanding access to primary education, improving vocational training in the modern industrial and commercial sectors, and training of lower secondary school teachers to replace a substantial number of foreign technical assistants. Future IDA assistance should continue to focus on the need to reduce expensive technical assistance personnel. The Government recently requested the Association to assist the Government Education Reform Committee in the definition of overall long-term objectives, and the formulation of policies.

Assistance to agriculture will continue because this sector is still considered Mauritania's principal source of long-term growth, despite its weak base and extreme vulnerability to drought, and the high cost of investments due to difficult physical conditions, limited transport infrastructure, and the high level of technical assistance needed. Through the Second Technical Assistance to the Rural Sector Project (FY 1983), rural institutions are being strengthened and efficient incentives developed by addressing such fundamental issues as input and product pricing, subsidies and land tenure.

A sector study has been prepared to assist the Government in the elaboration of a strategy in the fisheries sector, which could be an important source of future growth. The objective is to enable Mauritania to capture a larger share of the benefits currently reaped by foreign trawlers operating along the coast. Once this sector strategy is in place, a fisheries project could be considered.

In the energy sector, assistance from the World Bank Group consists of supporting the Government's search for oil through the Petroleum Exploration Project (FY 1982) and carrying out an energy assessment.

The Bank Group is also helping Mauritania to develop an overall strategy for the urban sector. Urbanization has accelerated dramatically in recent years, but appropriate measures to adjust to this development have not been taken.

To assist in Mauritania's efforts to diversify employment and sources of income, financing was provided through the Mauritanian Development Bank to encourage private enterprise and to promote artisanal carpet-weaving activities. A Second Industrial Development Project approved by the Board in FY 1985 is continuing to develop appropriate policies for improving subsector performance and assess the possibilities for further expansion of the manufacturing sector.

MAURITANIA--Basic Data

Area, population, and GDP per capita

Area:		1.0 million square kilometers
Resident population:	Total (1984):	1.7 million
	Growth rate:	2.4 percent
GDP per capita (1984):		SDR 410

	1981	1982	1983	1984 Prov.	1985 Proj.
GDP (at 1982 market prices)					
Total (in millions of ouguiyas)	39,692	38,838	41,401	41,190	42,220
Agriculture and livestock (in percent of total)	24.9	25.5	24.6	20.5	19.4
Fishing (in percent of total)	4.0	4.5	7.8	6.7	7.5
Mining (in percent of total)	11.0	9.2	9.3	14.1	14.4
Manufacturing (in percent of total)	3.3	3.2	3.1	3.3	3.4
Government (in percent of total)	11.2	12.2	12.8	13.0	12.9
Annual real rate of growth (percent)	3.7	-2.2	6.6	-0.5	2.5
Investment (in percent of GDP)	41.9	47.1	17.9	22.4	21.4
Prices			(Percent change)		
GDP deflator	7.0	9.9	4.0	11.2	11.6
Consumer price index (lower-income group)	11.5	8.4	4.9	8.0	12.0
Central government finance			(In millions of ouguiyas)		
Recurrent revenue	6,665	7,211	8,935	10,296	12,348
Foreign grants	5,035	4,627	4,382	6,027	7,184
Total expenditure	13,357	16,302	18,156	19,944	21,708
Recurrent	(9,579)	(10,881)	(12,791)	(12,499)	(15,424)
Development	(3,778)	(5,421)	(5,365)	(7,445)	(6,284)
Overall deficit (-) (commitment basis)	-1,657	-4,464	-4,839	-3,621	-2,176
Changes in arrears (decrease (-))	436	498	449	649	-8,371
Overall deficit (-) (cash basis)	-1,221	-3,966	-4,390	-2,972	-10,547
Foreign financing (net)	3,844	5,411	4,316	3,324	-1,067
Domestic borrowing	-2,623	-1,445	74	-352	--
Of which: from banking system	(703)	(426)	(1,458)	(-125)	(--)

MAURITANIA - Basic Data (continued)

	1981	1982	1983	1984	1985 Proj.
Money and credit			(Percent change)		
Domestic credit	15.8	21.3	10.0	9.3	5.5
Government	(27.5)	(13.1)	(39.6)	(-2.4)	(--)
Private sector	(12.5)	(23.9)	(1.5)	(13.9)	7.4
Money and quasi-money	33.2	-2.0	9.1	9.0	14.3
Balance of payments			(In millions of SDRs)		
Exports, f.o.b.	229.7	216.5	295.0	286.6	316.8
Imports, f.o.b.	-328.6	-384.8	-353.8	-294.7	-306.3
Trade balance	-99.0	-168.3	-58.8	-8.1	10.6
Services and private transfers (net)	-121.6	-179.1	-222.8	-227.7	-190.7
Sub-total	-220.6	-347.4	-281.6	-235.8	-180.1
Public transfers	85.5	77.6	74.0	97.6	97.5
Current account	-135.1	-269.8	-207.6	-138.2	-82.6
Capital account	111.6	163.7	124.7	31.8	6.1
Disbursements	(114.3)	(171.7)	(169.4)	(103.5)	(74.8)
Amortization	(-58.5)	(-43.4)	(-54.6)	(-69.4)	(-71.2)
Other capital	(55.8)	(35.4)	(9.9)	(-2.3)	(2.5)
Overall balance 1/	-23.5	-106.1	-82.9	-106.4	-76.5
Current account deficit as percent of GDP	21.2	39.9	28.2	19.6	12.3
Gross official foreign reserves (end of period)	142.9	129.8	105.4	82.7	82.7
In months of imports	5.2	4.0	3.6	3.4	3.0
External public debt					
Debt outstanding (end of period)	757.9	976.4	1,163.0	1,223.5	1,321.3
Debt service (in percent of exports of goods and services) 1/					
Excluding the Fund	29.2	28.4	28.0	34.5	32.0
Including the Fund	31.5	29.7	30.3	38.4	36.0

1/ Before debt relief.

MAURITANIA - Basic Data (concluded)

IMF data

Date of membership	September 10, 1963
Quota	SDR 33.9 million
Exchange rate (as of June 30, 1985)	
U.S. dollar/Local currency	US$1 = UM 80.15
SDR/Local currency equivalent	SDR1 = UM 79.91

	As of August 31, 1985 (In millions of SDRs)
Total outstanding purchases	29.08
Under tranche policies	29.08
Ordinary	(15.76)
Supplementary	(13.32)
Compensatory financing	--
Total Fund currency holdings (in percent of quota)	185.81
Net cumulative SDR allocation	9.72
Holdings of SDRs	--
Trust Fund loans outstanding	9.21

MAURITANIA - Statistical Issues

1. Outstanding statistical issues

a. Real sector

(i) National accounts statistics

The Statistics Directorate recently published official national accounts estimates for the period 1979-83, based on the recommendations of an EEC/UN-financed expert. However, the authorities acknowledge that further improvements in national accounts compilation are necessary. The Fund and World Bank staffs have jointly produced national accounts estimates for the period 1981-85 on the basis of a commonly agreed data base and methodology; these estimates were used in the Fund's reports on the Article IV consultation and review and in Mauritania's medium-term adjustment program sponsored by the World Bank.

(ii) Consumer price statistics

The mission noted a substantial deterioration in recent months in CPI compilation by the Directorate of Statistics. The authorities acknowledged that the reliability of the CPI as presently calculated by the Statistics Directorate was questionable and therefore requested technical assistance to improve CPI compilation before the second program review scheduled for December 1985. The staff supported this request, which was conveyed to the Fund's Bureau of Statistics.

b. Government finance

Under Mauritania's stand-by arrangement, the authorities are required to prepare a consolidated budget for 1986 which would include foreign-financed extrabudgetary operations. Because Mauritania lacks the necessary expertise to prepare such a budget, the authorities requested Fund technical assistance in this area as well; the Fund's Fiscal Affairs Department is expected to accede to this request by sending an evaluation mission to Nouakchott.

Information on Treasury operations is expected to be improved in the near future as a result of a long-term technical assistance project sponsored by the French Government in the Ministry of Finance and Commerce. Implementation of a new public accounting framework and a statistical framework for monitoring Treasury operations is already under way. The Ministry of Finance and Commerce has also benefitted from a Bureau technical assistance mission in February 1985 whose aim was to improve the compilation of Statistics on Treasury operations in accordance with the GFS format.

c. Money and banking

A Bureau technical assistance mission on monetary statistics took place in November 1984; based on the mission's findings, a detailed Bureau report recommending improvements in monetary statistics compilation methods is expected to be forwarded to the authorities shortly. The staff emphasized the urgent need to improve the recording of non-performing loans and external short-term credit because of their possible impact on credit performance criteria.

d. External sector

(i) External trade statistics

Although major efforts are under way at the Customs Directorate to improve external trade data compilation, no set of data on a transaction basis has been made available to date. Therefore, the staff had to rely on trade estimates based on foreign exchange records maintained by the Central Bank; however, these estimates lack price and quantity information.

(ii) Balance of payments statistics

Balance of payments data are fairly detailed and up to date. However, improvement is still needed in the recording of workers' remittances, food aid flows, and imports financed through short-term credits.

(iii) External debt statistics

The staff had to rely on the external debt statistics as compiled under the World Bank's Debt Reporting System (DRS). Due to Mauritania's need for gap-fill exercises, it is imperative that an accurate picture of debt servicing obligations be provided on a regular basis. In this regard, an external debt management expert is scheduled to be assigned to Nouakchott in the coming months under the technical assistance program monitored by the Fund's Central Banking Department.

2. Coverage and currentness in reporting of IFS data

In the table below, the data appearing on Mauritania's country page in the September 1985 issue of IFS are compared with the data provided to the consultation and review mission in respect of coverage and currentness. The data in IFS are based on reports sent to the Fund's Bureau of Statistics by the Central Bank of Mauritania, which during the past year have been provided on a fairly timely basis.

		Latest data in September 1985 IFS	New official data obtained by the Article IV consultation and review mission
Real sector -	National accounts	1980	1983
	Consumer price index	December 1984 1/	June 1985 2/
	Production	n.a.	1984 3/
	Employment	n.a.	n.a.
	Earnings	n.a.	1985
Government finance	- Deficit/Surplus	1979	1984
	Financing	1979	1984
	Debt	--	1984
Monetary accounts	- Central banks	April 1985	April 1985
	Deposit money banks	April 1985	April 1985
	Other financial institutions	n.a	--
External sector	- Merchandise trade:		
	Values	January 1985	--
	Prices	n.a.	
	Balance of payments	1983	1984
	International reserves	June 1985	June 1985
	Exchange rates	June 1985	June 1985

1/ Refers to expatriate consumption patterns; compilation of this CPI was discontinued in early 1985.

2/ Refers to Mauritanian consumption patterns for low-income earners in Nouakchott.

3/ Incomplete coverage.