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SM/85/203
Supplement 1*

CONTAINS CONFIDENTIAL
INFORMATION

August 8, 1985

To: Members of the Executive Board
From: The Secretary
Subject: Somalia - Staff Report for the 1985 Article IV Consultation

The attached supplement to the staff report for the 1985 Article IV consultation with Somalia has been prepared on the basis of additional information.

Mr. Ewart Williams (ext. 6973) or Ms. Calika (ext. 6948) are available to answer technical or factual questions relating to this paper prior to the Board discussion tomorrow, Friday, August 9, 1985.

Att: (1)

* Reissued: 8/8/85

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INTERNATIONAL MONETARY FUND

SOMALIA

Staff Report for the 1985 Article IV Consultation

Supplementary Information

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 A.D. Ouattara and W.A. Beveridge

August 8, 1985

The following updates the discussion presented in the Staff Report for the Article IV consultation (SM/85/203) in a few major areas.

1. Stand-by review

It was noted in the staff report that the mid-term review of the current stand-by arrangement for Somalia was initiated at the same time as the Article IV consultation discussions were being conducted. A follow-up mission which visited Somalia in the period June 27-July 4 was not able to complete the review because understandings could not be reached on a package of measures considered adequate to correct for the slippages in the first half of the year and to prevent the program from going further off track. Further contacts are expected to take place with the authorities in late August.

At the present time Somalia has accumulated overdue financial obligations to the Fund amounting to SDR 6.8 million.

2. Exchange rate developments

The last occasion on which the official exchange rate was depreciated in accordance with the formula adopted by the authorities in the context of the economic program for 1985 (i.e., adjustment to the real SDR plus a discrete devaluation of So. Sh. 0.5 per U.S. dollar once a month) was in mid-May in respect of the month of April. At that time the exchange rate was depreciated from So. Sh. 37.5 per U.S. dollar to So. Sh. 40.1 per U.S. dollar. As at mid-July 1985, the official exchange rate was So. Sh. 40.6 per U.S. dollar as compared with So. Sh. 48.3 per U.S. dollar which should have been the rate, given the adjustment formula of the program. Meanwhile, the weighted average exchange rate in the

free market rose from So. Sh. 95 per U.S. dollar in mid-May to So. Sh. 103 per U.S. dollar as at mid-July. The spread between the official and free market rates thus continued to widen considerably.

3. The official exchange market

The situation in the official foreign exchange market has continued to deteriorate. As at the end of June official reserves had been virtually depleted, US\$15 million of external payments arrears outstanding as at end-1984 had not been eliminated as provided for under the stand-by arrangement, and in addition new debt servicing arrears of US\$9 million had been accumulated.

For the year as a whole, the imbalance in the official foreign exchange market, taking into account the programmed accumulation of gross official reserves of US\$33 million (as provided in the program), is now estimated at US\$70 million, as against US\$60 million cited in the staff report (Table 1). The revision to the earlier projections stems from (i) another US\$4 million of oil purchases through the official market and (ii) a further downward revision of likely inflows to embassies and international institutions (from US\$16 million to US\$10 million) and in net export receipts surrendered (from US\$35 million to US\$29 million). The latter reflects some underinvoicing of export earnings related to the large differential between the official and free market rates as well as deductions from the earnings of exports shipped to Egypt to cover previously unrecorded debt service obligations. These were partly offset by a downward revision of scheduled amortization payments. As discussed in the staff report, this gap would need to be closed mainly by (1) further debt rescheduling and (2) government purchases of foreign exchange from the free market. A marginal contribution toward closing the gap is expected to come from a reduction in government imports and service transfers abroad.

4. The balance of payments outlook for 1985

The revised balance of payments outlook for 1985 is shown in Table 2. The program had envisaged a current account deficit of US\$131 million and an overall balance of payments surplus of US\$18 million. Reflecting shortfalls in certain official inflows and higher projections for debt servicing, the balance of payments projections were revised in SM/85/203 to show a current account deficit of US\$126 million and an overall balance of payments deficit of US\$47 million. Due to additional downward revision of official inflows and export receipts as mentioned above, the current account deficit of the balance of payments is now projected at US\$140 million and the overall deficit at US\$68 million.

5. Performance criteria

As mentioned earlier the performance criterion on the stock of external payments arrears was not observed as at the end of June 1985 as Somalia did not eliminate arrears outstanding as at the end of 1984. Indeed new external payments arrears were accumulated in the first half of 1985. Data for the banking system for end-June have not yet been received but after allowance for the domestic counterpart of the accumulation of external arrears, it is projected that both the program ceilings on net domestic credit and on net bank credit to the Government have been exceeded. In addition, as mentioned earlier, the review scheduled before June 1985 was not completed and Somalia has become overdue in its obligations to the Fund.

Table 1. Somalia: Official Foreign Exchange Market, 1985

(In millions of U.S. dollars)

	According to SM/85/203	Revised
<u>Receipts</u> ^{1/}	<u>172.5</u>	<u>161.2</u>
Saudi cash grants	40.0	41.0 ^{2/}
IMF purchases	50.0	50.0
AMF purchases	4.0	4.0
Other grants (oil and freight)	27.5	27.5
Export receipts surrendered	35.0	28.7
Service receipts (embassies)	16.0	10.0
<u>Payments</u>	<u>200.1</u>	<u>198.7</u>
Discharge of arrears	41.3	41.3
Of which: already paid	(25.8)	(25.8) ^{3/}
still to be paid	(15.5)	(15.5)
Debt servicing, excluding IMF	44.0	38.8
Of which: moratorium interest	(10.0)	(10.0)
debt falling due in 1985	(30.0)	(24.8) ^{4/}
AMF purchases and charges	(4.0)	(4.0)
IMF repurchases and charges	27.3	27.3
Oil imports	50.0	53.8 ^{5/}
Other government imports	10.0	10.0
Embassy expenses and freight	23.0	23.0
Government travel and others	4.5	4.5
<u>Balance</u>	<u>-27.6</u>	<u>-37.5</u>
<u>Targeted reserve accumulation</u> ^{6/}	<u>33.0</u>	<u>33.0</u>
<u>Financing gap</u>	<u>60.6</u>	<u>70.5</u>

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

^{1/} Includes grants and loans under negotiations.

^{2/} In addition to Saudi grants of US\$40 million, a cash grant of US\$1 million was received from Qatar in May.

^{3/} Includes payments due to Irving Trust and Saudia, some of which has not been paid.

^{4/} Revision necessary as debt service to Islamic Development Bank of current maturities amounting to US\$5.19 million that had been rescheduled was erroneously included under arrears outstanding as of end-1984 that were rescheduled (i.e. included in the sum of US\$12.5 million).

^{5/} Revision necessary as oil imports already paid or committed during January-May 1985 amounted to US\$31.3 million. Together with US\$22.5 million in oil imports financed through CIP total oil imports amount to US\$53.8 million.

^{6/} Targeted reserve accumulation according to the arrangement as originally adopted. The balance of payments projections assume a reserve accumulation of US\$15 million.

Table 2. Somalia: Balance of Payments, 1981-85
(In millions of U.S. dollars; unless otherwise stated)

	1981	1982	1983 Rev.	1984 Prel. Act.	1985 Prog. 1/	1985 Rev. Est.
Goods and services (net)	-309	-338	-346	-391	-480	-497
Exports, f.o.b. 2/	114	137	100	62	109	97
Livestock	98	106	72	33	78	64
Bananas	6	14	15	14	14	15
Others	10	17	13	15	17	18
Imports, c.i.f.	-422	-484	-450	-406	-570	-536
Foreign exchange 2/	-145	-199	-186	-105)		
Foreign currency accounts	--	-5	-20	--)	-220	-171
Franco valuta 2/	-60	--	--	-51)		
Grants in kind	-140	-157	-147	-151	-229	-236
Loans in kind	-77	-123	-97	-99	-121	-129
Trade balance	-308	-347	-350	-344	-461	-439
Net services	-1	9	4	-47	-19	-58
(Nf which: interest payments)	(-10)	(-14)	(-6)	(-44) 3/	(-31) 3/	(-50) 3/
Transfers	214	207	199	246	349	357
Private	64	50	51	72	80	80
Official, of which	150	157	148	174	269	277
Saudi cash grant	(--)	(--)	(--)	(20)	(40)	(40)
Other cash	(10)	(--)	(1)	(3)	(--)	(1)
Current account balance (excluding official transfers)	-95	-131	-147	-145	-131	-140
Capital account	79	84	68	23	94	72
Private	--	-39	-32	-23	--	-7
Official (net)	79	123	100	46	94	79
Disbursements	(93)	(132)	(107)	(106)	(121)	(129)
Amortization	(-14)	(-8)	(-6)	(-59) 3/	(-27) 3/	(-50) 3/
Capital subscriptions and others	(--)	(-1)	(-1)	(-1)	(--)	(--)
Gap-fill financing	...	...	...	...	55	...
Errors and omissions	3	3	-7	-17	--	--
Overall balance	-13	-44	-86	-139	18	-68
Financing	13	44	86	139	-18	68
Central Bank, net 4/	33	64	47	13	-3	20
Assets	-17	28	-1	9	-33	-15
Liabilities	50	36	48	4	30	35
Of which:						
Use of Fund credit	(30)	(34)	(44)	(-3)	(35)	(35)
Purchases	(30)	(34)	(44)	(--)	(50)	(50)
Repurchases	(--)	(--)	(--)	(-3)	(-15)	(-15)
Commercial bank, net 4/	-20	-20	39	29	--	2
Accumulation of arrears (New arrears)	--	--	--	97	-61	-112
Italian suppliers	...	...	...	(...)	(...)	(13)
Other debt service	...	...	...	(45)	(...)	(-62)
Commercial	...	...	...	(52)	(-51)	(-36)
Arrears already rescheduled	...	...	...	...	(-10)	(-27)
Arrears yet to be settled	--	--	--	--	24	97
Current debt service rescheduled	...	...	...	...	...	15
rescheduled	--	--	--	--	22	46
Memorandum items:						
Gross official reserves (In weeks of cash imports) 5/	42	14	16	6	39	21
	10.7	3.6	4.0	2.0	9.2	6.9

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

1/ On the basis on which the program was approved.

2/ Data differ somewhat from information on foreign exchange flows. Adjustments were made based on other sources of information, reflecting changing lag structure between trade and foreign exchange flows.

3/ On the basis of known scheduled payments; not comparable with data for previous years which refer to actual debt service payments made and exclude other scheduled payments due but not paid.

4/ Including revaluation due to exchange rate movements.

5/ Comprising foreign exchange, franco valuta, and foreign currency account imports.

