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Series:	Operations Committee records of the Chairman (Moeen Qureshi)
Dates:	06/19/1989 - 07/24/1989
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M- QURESHI'S
OPERATIONS CMTE

June 23 - July 1989

July 26, 1989

THE WORLD BANK

Operations Committee

CONFIDENTIAL

SUDAN

COUNTRY STRATEGY PAPER

Postscript

6.01 The Region highlighted the strategy proposed, indicating that the core program represented little more than a holding operation to maintain a dialogue on economic reform. Set at about a third of the country norm, the program recognizes that the structural changes required to vitalize the Sudanese economy are unlikely to materialize in the near future, considering political uncertainties and government instability, the problems of the South, the substantial debt overhang and the mounting service arrears, including $1 billion to the IMF. The size of the lending program was modest enough not to discourage Sudan from seeking agreement with the Fund. In reaction to a question by the Chairman as to whether Sudan was sufficiently stable for the Bank to formulate a meaningful assistance strategy at this time, the Region said that the new military government was facing great difficulties, and that its recognition, which remained limited, was increasing, albeit slowly. Until the civil war in the South is settled no stability can be expected. The government has assured the Bank that it will continue to honor all its obligations, and the strategy proposed was flexible enough to deal with the prevailing uncertainties.

6.02 A member queried the Highway Rehabilitation Project for $83 million in FY90 which would raise the lending program in that year to $126 million, before it falls to $50 million in each of the following two years. The Region explained that that project was a carry-over from FY89, having been deferred pending finalization of cofinancing arrangements. The Region added that the project was vital as it concerned the country's life line for transportation between Khartoum and Port Sudan; that part of the project was related to flood reconstruction; and that by addressing the issue of cost overruns in an earlier Bank-financed highway project it was likely to facilitate the resumption of bilateral German aid which had been suspended. A special effort will be made to ensure that operations and maintenance needs are met. Another member noted the fact that the Region saw no prospects for macroeconomic reform, and asked if minor improvements were still possible. Yet others raised the question of the productivity of new investments versus maintenance of old capital, and whether as the Agenda had indicated, the projected inflow of debt creating funds was realistic. The Region reiterated that the chances were indeed slim for comprehensive macroeconomic reforms any time soon. However, it was likely that Sudan would at least embark on periodic ad hoc measures to avert a complete macroeconomic breakdown and the Region intends to use its economic and sector work to encourage the Government to embark on comprehensive reforms without delay. The debt burden was so large that a great deal of time and resources were necessary to affect it. In a certain sense, the Region added, Sudan is better off muddling through as at present, with arrears mounting and being tacitly accepted, than with a formal solution whereby the creditors are repaid without the money ever reaching Sudan. With regard to the core program the Region explained that it focused essentially on human resource development, maintenance of infrastructure, and other long-term development projects. A member commented that support for infrastructure projects was necessary to elicit a better supply response when reforms are undertaken.

6.03 Another member noted that the Bank seems no longer to have any leverage on Sudan, and that expectations that Sudan would become the bread basket for the Gulf area have been disappointed and lie at the heart of the creation of the debt problem. Another said that a write-off of much of the debt was the only solution. To a question raised by another member as to whether adjustment was possible in the shadow of the debt problem, the Region said that adjustment was needed whether or not there was a debt problem.

6.04 A member thought that a smaller core program than the one suggested was more appropriate, considering also the arrears to the Fund. The Chairman thought that arrears to the Fund constituted a problem that caused concern to the Bank and that we should continue to bear it in mind in our dealings with Sudan. However, since the proposed lending was not large enough to discourage Sudan from talking to the Fund, it should be regarded as unexceptional.

6.05 In conclusion the Committee endorsed the strategy proposed, with a lending program of about $50 million a year for FYs 90-94 (in addition to the FY90 highway project) addressing institution building and human resource development, poverty alleviation, food security and the environment, and with a strengthened CESW to sustain the dialogue on reform. The Committee did endorse the proposal (para. 1.11) that the local cost financing guidelines established for Sudan in December 1985, would remain in force with an 80% IDA maximum share in total project cost, rising to 90% for all donors in cases involving external financing. Criteria for local cost financing should not be decided on a case by case basis, the Chairman said, but should await a forthcoming study setting such guidelines Bankwide.

August 7, 1989

SES
SESerafy/lcu

LIST OF PARTICIPANTS ATTENDING THE OPERATIONS COMMITTEE MEETING

SUDAN: COUNTRY STRATEGY PAPER

WEDNESDAY, JULY 26, 1989, AT 3.30 P.M. IN ROOM E-1243

Committee Members

Messrs. A. Karaosmanoglu, Chairman
E. Jaycox, AFRVP
S. Husain, LACVP
J. Wood, FPRVP
H. Scott, LEGVP
E. Stoutjesdijk, EMNVP
J. Linn, DECVP

Other Attendees:

Messrs. Y. Ansu, AF2CO
R. Armstrong, AFRCE
H. Gruss, LEGAF
S. El Serafy, EAS
A. Heron, CODOP
J. Katz, FRM
C. Madavo, AF2DR
M. Muhsin, AF2CO
C. Obidegwu, SPRPA
Mrs. N. Okonjo-Iweala, OPNSV
S. Rajapatirana, EAS
A. Steer,FRS

THE WORLD BANK

Operations Committee

CONFIDENTIAL

ETHIOPIA

COUNTRY STRATEGY PAPER

Postscript

78. The Region summarized the strategy it proposed, laying stress on strengthening the country economic and sector work in support of the policy dialogue. A small core lending program would address poverty and long-term development, to be expanded to an enhanced core only in response to sectoral reforms. Members expressed concern about the high defense expenditure (about 13% of GNP) which preempts resources that should be devoted to development, and might imply that donors are financing the war. The same concern was reiterated with special reference to donors' contributions to IDA which are predicated on rigorous performance standards, and to the desire that uniform criteria should determine lending levels Bankwide. On the other hand, the Region stated that serious efforts were being made by the government to conclude the military conflict, and that Soviet aid, which has been sustaining the government's war efforts, would be scaled down. The Chairman, while showing sympathy for members' reservations, expressed the view that judging the proper level of military expenditure was difficult for outsiders; that the core lending program proposed was at a much lower level than previous lending; and that there seemed to be merit in the argument that a foot-in-the-door lending strategy was necessary and could be productive. The Region argued that the country had been feudal until recently, is current in meeting its debt service obligations, and that progress could be pursued on deregulation and privatization in association with the core program.

79. At the behest of the Chairman the Committee considered the level of lending, the composition of the core program, and the conditions that should govern the continuation, increase or decrease of the core program. Members stressed the absence of clear information on the use of domestic resources, some strongly advocating one operation a year as the core appeared to them to be too large. These argued that the government should be urged to reallocate expenditures and sustain a reasonable level of investment. Was the core program viable in the current domestic policy environment? A member enquired. The Region stated that the dialogue was promising and that the core would continue only if it was viable and contributed to the country's long-term socio-economic development. To slow down lending now much below the proposed core was likely to give the wrong signals. The Chairman indicated that it was perhaps easier for the government to move on policy reforms than on military matters, and our program should respond to that. The Region stressed that even the core lending would be cut unless there was progress towards ending the war.

80. The Region added that reforms would take time to produce results; that some $90 million a year of lending in the current and next years falls well below lending in the past three years, which was not divided between core and non-core; and that the next CSP was planned for March 1991. A member said that high lending in the past was based on false expectations and should not be used as a platform for the core program: one operation and $50 million represented to him the proper level of lending, but the Region was adamant that the norm was considerably higher than the proposed program, and that a level of lending equivalent to 90 cents per capita was highly inadequate and was not likely to bring about the results being sought.

81. The proposal made in para. 77 to the effect that IDA's share in financing project cost be raised to 90% was not adopted. Instead, the Committee decided that the guidelines for local cost financing for Ethiopia, established in August 1968, should remain in force until such a time that a Bankwide study of cost sharing has been carried out. For Ethiopia the old guidelines set maximum IDA share at 75% of total project costs. The old guidelines had also set total external financing, where co-financing was involved, at a maximum of 90% of total project costs.

82. Summing up the decisions of the Committee the Chairman said that he sensed that the Committee was divided on the appropriate level of the core lending program, with strong feelings that it should be reduced. He thought that instead of reviewing the lending program in two years, as proposed, this should take place one year from now. Meanwhile, until the level of lending to Ethiopia is decided in the context of the Bankwide IDA allocation exercise, IDA should be prepared to adjust the level of lending in response to policy change. Issues to decide the level of lending would include expenditure allocations, export orientation of policies, and the exchange rate.

August 7, 1989

SES

SESerafy/lcu

LIST OF PARTICIPANTS ATTENDING THE OPERATIONS COMMITTEE MEETING

ETHIOPIA: COUNTRY STRATEGY PAPER

WEDNESDAY, JULY 26, 1989 AT 3.30 P.M. IN ROOM E-1243

Committee Members

Messrs. A. Karaosmanoglu, Chairman
E. Jaycox, AFRVP
S. Husain, LACVP
J. Wood, FPRVP
H. Scott, LEGVP
E. Stoutjesdijk, EMNVP
J. Linn, DECVP

Other Attendees:

Messrs. R. Armstrong, AFRCE
S. Choi, AF2CO
S. El Serafy, EAS
A. Heron, CODOP
J. Katz, FRM
C. Madavo, AF2DR
K. Newcombe, AF2IE
C. Obidegwu, SPRPA
Mrs. N. Okonjo-Iweala, OPNSV
S. Rajapatirana, EAS
J. Roberts, AF2CO

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

8907240091.

DATE: July 24, 1989

TO: Operations Committee

FROM: Sarath Rajapatirana, Acting Director, EAS

EXTENSION: 78057

SUBJECT: ETHIOPIA - Country Strategy Paper
- Agenda

1. The Operations Committee will meet on Wednesday, July 26, at 2.30 p.m. in Room E-1243 to consider the Ethiopia CSP. The Committee may wish to take up for discussion the issues identified in this agenda.

Background

2. One of the poorest countries, with a population of 47 million growing at 3% a year, and with an income per capita of about $120, Ethiopia has been prone to droughts, famines and civil wars. With a stagnant or near-stagnant output in the recent past, standards of living have been falling. Savings and investments are extremely low, and consumption in 1986 (the last firm year of national accounts) was 99% of GDP. However, fiscal policy has tended to be conservative, with consumer prices rising only at 4% a year between 1980 and 1987. Owing largely to an unbalanced foreign trade, the balance of payments current account has been in deficit by nearly $500 million a year (about 9% of GDP) over the past three years. External debt is about half of GDP, and debt service is estimated at 37% of exports in 1989. The official exchange rate, constant in nominal terms for several years, is overvalued by about 50% and is kept in place by strict administrative controls. Eighty percent of the labor force (of about 20 million) is in agriculture, and the social indicators are very depressed or otherwise unknown (Annex C). Things would have been worse without generous external assistance which is now showing signs of weakening. Government energies and resources have increasingly been absorbed by military conflicts, with security expenditure now amounting to half the current budget.

3. Ethiopia is current in meeting its repayment obligations to the Bank, IDA and the IMF as well as other private and official creditors. State intervention in the economy is pervasive, and a dualistic system has developed whereby private sector activities have higher prices. Open unemployment is rising, particularly in the urban centers and even among the few secondary-school educated. Controversial programs of land nationalization, peasant settlements and population resettlements from drought prone and overpopulated areas have been in progress. Despite recent defeats in the war against Eritrean and Tigray nationalists, no end of the civil war is in sight, and an attempted army coup in May was crushed. IDA lending averaged nearly $100 million a year in FY87 and FY88, and this rose to $157 million in FY89 for two projects in transport and peasant agriculture.

- The Region might give an update of the political situation in the wake of the attempted May coup, indicating any recent developments on the civil war front, the impact of the political situation on economic policy and the status of the dialogue between the Bank and Ethiopia.

Development Issues and the Lending Strategy

4. The CSP identifies several constraints on Ethiopia's development viz: land shortage, climate, (over)population, skills, (low) investment, institutions, inadequate incentives and the war, adding that economic reforms can only partially mitigate these. The need to develop human resources is stressed in the CSP, to raise education and the formation of skills, reduce population growth and redistribute people from the rapidly eroding highlands of the north. The analysis of poverty, food security, and the environment in the CSP is not forced, but flows smoothly from the identification of constraints and the exploration of development prospects. The Region, however, seems constrained in developing a full program that would address the identified long-term development needs by the inadequacy of the macroeconomic framework and Ethiopia's political difficulties. ("Core development projects will only be chosen if they are viable in the imperfect policy environment..." para. 69.) While lending could conceivably rise to $250 million a year, the core lending program proposed averages $96 million a year in the quinquennium FY90-94 for 10 projects addressing food security, forestry, transport, urban development population, education and institutional development, with an enhanced core program adding an average of $72 million a year for peasant farming, industry and energy development. The change from the core to the high core scenario would be triggered by policy change in the sector concerned, with a yet higher lending level envisaged, including adjustment operations, consequent upon reforms of the exchange rate and liberalization of pricing and marketing.

- The Region might clarify the policy differences between the core, the enhanced core and the higher lending programs proposed, and describe the trigger mechanisms that would activate higher lending scenarios.

- Is full lending up to Ethiopia's norm at all possible in the foreseeable future? Would it not be possible to work constructively on many of the long-term development constraints, so clearly identified in the CSP, irrespective of the policy climate?

Economic and Sector Work

5. The Region is programming some 240 staffweeks a year for economic and sector work on Ethiopia in FYs 90-92. About 30% of this work is not identified by task.

- The Region might shed light on the tasks to be addressed and the Committee might wish to discuss the adequacy of this level of resource use.

Local Cost Financing

6. The CSP is proposing that IDA finance 90% of total project costs (less duties and taxes) whether or not cofinancing is present. This proposal seems in line with Ethiopia's conditions and with comparable country situations (though 80% is proposed for Sudan for IDA-only projects.)

- The Committee might, however, consider if such financing should not be confined to the projects under the core lending program, with the 75% maximum of IDA-only lending applying to non-core lending while continuing to finance up to 90% of the costs of combined donor financing where cofinancing is involved.

Distribution

Messrs. Qureshi, OPNSV (o/r); Karaosmanoglu, ASIVP; Husain, LACVP; Jaycox, AFRVP; Thalwitz, EMNVP; Rajagopalan, PREVP; Fischer, DECVP; Shihata, LEGVP; Wood, FPRVP; Vergin, OPNSV.

cc: Messrs. Lee, COD; Shakow, SPR; Holsen, CEC; Rao, FRS; Burmester/Thahane, SEC; Liebenthal, SPRPA; Steer, FRS; Baudon, OPNSV; Hopper, PPRSV; Bock, DFS; Goldberg, LEGOP; Kavalsky, FRM; Parmar, IFC (CIO); Pfeffermann, IFC (CEI); Baneth, IEC; Robless, OPNSV; Ms. Haug, EXC; Tanaka, EXC; Aguirre-Sacasa, EXT; Agarwala, AFRCE; O'Brien, AFRVP; Madavo, AF2DR; Amoako, AF2CO; Lateef, AF2CO.

SESerafy/lcu

July 24, 1989

THE WORLD BANK
OPERATIONS COMMITTEE

CONFIDENTIAL

COSTA RICA

COUNTRY STRATEGY PAPER

Postscript

89. The Operations Committee met on July 24, 1989 to discuss the Country Strategy Paper for Costa Rica.

90. The discussion focussed on Costa Rica's performance and prospects, and on financing requirements. It was noted that Costa Rica has consistently been a good performer since the crisis of the early 1980s, and it has outstanding achievements to its credit in the social and political areas--for example, the virtual absence of defense spending, the tradition of democracy, high levels of education and health, etc. At this time the IMF is also satisfied with Costa Rica's short-term performance indicators. As far as the adjustment program is concerned, many of the SAL II policy measures are being implemented in any event despite the delay in the ratification by the Assembly and trade liberalization is proceeding apace. The Government's commitment to the reform program remains strong.

91. The reasonableness of the financial work-outs was questioned, particularly with reference to Table 3, on page 18. It was pointed out that these amounts seem large because they are in gross terms; the projections include interest payments and clearance of arrears on interest. Questions were raised regarding the assumptions concerning closure of the estimated financial gaps; given that about half of the gap would need to be closed through new concessional funds, what would be the fall-back position if such funds were not forthcoming? It was suggested that Costa Rica is a unique case and enjoys special good will; the relevant options are the continuation of the present situation with accumulated arrears or a debt agreement - there is no question of Costa Rica being obliged to pay. As the best performing small country in the LAC region, Costa Rica also deserves priority in the provision of concessional finance, as the Bank would make clear at the next Consultative Group meeting. It was suggested that the statements on the likely effects of underfunding in paragraph 61 be revised; it was also suggested that a conversion of Table 3 to a net basis be considered.

92. The case for postponing adjustment lending until FY92 was also discussed. The Region said that the various components of SAL II will support adjustments which will link up with FY90 and FY91 investment loans to transport, education and agriculture. Furthermore, elections will be held in February 1990, and the new Government will take office in May 1990; discussions on policy-based lending will therefore start only in early FY91.

93. Regarding environment it was suggested that fundamental improvements are unlikely unless effective action is taken to reduce population pressures and to bring under-exploited arable land into more productive use. Progress on these issues will not be easy. However, the Government is committed to environmental improvements, and the Bank will raise these issues with the Consultative Group and seek donor support for the Government's initiatives. On cost-sharing, it was decided not to increase the ceiling until the completion of a review by the Central Operations Department.

ARay:vlw
July 24, 1989

LIST OF PERSONS ATTENDING THE OPERATIONS COMMITTEE MEETING

COSTA RICA - COUNTRY STRATEGY PAPER

MONDAY, JULY 24, 1989 AT 10:30 A.M. IN ROOM E-1243

Committee Members

Messrs.	A. Karaosmanoglu	- Chairman
	S. Husain	- LACVP
	E. Jaycox	- AFRVP
	A. Stoutjesdijk	- EMNVP
	J. Linn	- DECVP
	D. Goldberg	- LEGVP
	J. Wood	- FPRVP
	H. Vergin	- OPNSV

Other Attendees

Messrs.	A. Ray (EAS)
	R. Martin (LACVP)
	R. Steckhan (LA2DR)
	L. Derbez (LA2CO)
	D. Yuravlivker (LA2CO)
Ms.	S. Augusto (LA2CO)
	F. Earwaker (SPR)
	D. Hanna (FRS)

8907190022 | MAQ

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: July 18, 1989

TO: Operations Committee

FROM: Vinod Dubey, Director, EAS V Dubey

EXTENSION: 78051/2

SUBJECT: COSTA RICA - Country Strategy Paper - Agenda

1. The Committee will meet on Monday, July 24, 1989 at 10:30 a.m. in Room E-1243 to discuss the Country Strategy Paper for Costa Rica.

2. In the late 1970s and early 1980s the Costa Rican economy suffered from significant deterioration in its external terms of trade, increases in international interest rates, and growing political and economic difficulties in the Central American region. Expansionary domestic policies led to inflation, real appreciations of the currency, and large increases in commercial borrowing. Stabilization policies produced a deep recession in 1982, but since then Costa Rica has managed to combine reasonable stability with positive growth rates, helped no doubt by the accumulation of arrears to commercial banks and bilateral creditors. The challenge is to maintain a growing economy while restructuring debt in such a way as to reduce the large debt overhang to normal proportions.

Issues

3. The base case leads to an unidentified financing gap of $247 million in 1989 and about $135 thereafter. This gap is supposed to be filled through higher levels of foreign private investments, larger bilateral assistance on concessional terms, and debt reduction, or, alternatively, through further accumulation of arrears. A low case is also presented which leads to a financing gap roughly double that in the base case. The Committee might consider:

- the reasonableness of constructing a base case that assumes "full implementation of the ongoing adjustment program (para. 7)." This assumption seems over optimistic given Costa Rica's record. Performance under SAL I was mixed and slower than expected; full compliance with the original conditions could not be secured. More recently there have been slippages in fiscal policies, and the end-1988 Fund targets on the deficit and on the central government expenditures were missed, as was the limit on domestic credit; inflation had been higher than expected;

- debt restructuring. The Region might elaborate upon its assumptions regarding how the financial gaps might get closed, the status of Costa Rica's discussions with the commercial banks, the prospects of increased concessional assistance, and the preparation for the debt buy-backs. Should there be a SAL-supplement for the set-aside?

- the downside. No indication is given as to how the much larger financial gaps implied by the low-case, which corresponds to discontinuities in the adjustment program, will get filled. If in addition one adds adverse external events - a 10% drop in the coffee price for example -- the risks appear greatly amplified. The downside costs may also have been somewhat understated because of the assumption that Costa Rica can continue to accumulate arrears without penalty (i.e., costs in terms of more expensive trade credit, reduced foreign private investments etc.). The Region might explain how it assesses the overall risks of underfunding, policy slippages, and external shocks, and what contingency measures might be appropriate;

- balance between adjustment and investment lending. The Region might explain why the share of adjustment lending has been fixed at 40% and how its timing (1992 on) has been determined;

- core programming. The Region might explain the "trigger" points, with reference to which we will downgrade our lending program. Is the failure by the Assembly to ratify SAL II one of the trigger points?

- is it a good idea to raise project cost-sharing from 50% to 75% (para. 86), the same treatment that many poorer IDA-only countries get? What specific counterpart-funding problems will be relieved thereby, and why cannot remedial measures be undertaken anyhow?

- how are the environmental concerns (para. 51) incorporated in our operations? While land taxes may be the best answer in principle, they have seldom been implementable in developing countries; in any event it is likely to be only one of many measures needed. What are the alternative strategies that should be considered?

OC Members

Messrs. Qureshi, Husain, Jaycox, Karaosmanoglu, Thalwitz, Rajagopalan Fischer, Shihata, Wood, Vergin.

cc: Messrs. Lee (COD); Shakow, Liebenthal (SPR); Holsen (CEC); Rao, Steer (FRS); Burmester/Thahane (SEC); Baudon (OPNSV); Hopper (PPRSV); Bock (DFS); Goldberg (LEGOP); Kavalsky (FRM); Parmar (CIO); Pfeffermann (CEI); Baneth (IEC); Robless (OPNSV); (Ms.) Haug, Tanaka (EXC); Aguirre-Sacasa (EXT); Barandiaran (LACVP); Steckhan, Martinez, Wijnbergen, LA2.

ARay:vlw

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THE WORLD BANK
OPERATIONS COMMITTEE

CONFIDENTIAL

JAMAICA

COUNTRY STRATEGY PAPER UPDATE

Postscript

45. The Operations Committee met on July 24, 1989, to discuss the Country Strategy Paper Update for Jamaica.

46. The discussion focussed mainly on the performance of the Jamaican economy, the central issue being the extent to which it can be attributed to domestic policy reforms rather than to fortuitous changes in the external terms of trade. The Region stated that up until the Hurricane Gilbert last year Jamaica's performance had exceeded expectations that we held two years ago in all respects, particularly growth of non-traditional exports and net inflow of foreign investments. The hurricane has set back progress but only temporarily. The ongoing structural transformation is best shown by the increases in the share of non-traditional items from 9% to 13%, and that of tourism and other non-factor services from 46% to 54%. Priorities at this point would be to sustain the broad policy framework, while maintaining a roughly constant level of Bank exposure.

47. In this context, progress on revenue-raising measures was discussed, especially the changes in the bauxite levy and the expected implementation of the general consumption tax by January 1990. The appreciation of the exchange rate in terms of non-dollar currencies was also noted. It was pointed out that the IMF has reached a new agreement on exchange rate management which involves quarterly triggers, the main one being the level of international reserves. The exchange rate will also have to be changed if auction arrears are not cleared up. Financial sector issues were also raised. It was suggested that the financial sector in Jamaica suffered from the same deficiencies as elsewhere - for example lack of long-term instruments, large and poorly targetted interest rate subsidies, forced investments etc. These issues would be addressed through the forthcoming trade and finance loan.

48. The question of debt restructuring was also raised, it being suggested by the Region that an approach similar to the one we are taking in Costa Rica might also be appropriate in Jamaica even though the share of commercial bank debt is about 10%. The initiation of a program of debt-equity swaps was also noted; the new administration has also expressed interest in exploring various debt reduction options. On the lending program, it was suggested that the lending strategy after the transition from adjustment lending into project lending be elaborated and the project pipeline strengthened.

ARay:vlw
July 24, 1989

LIST OF PERSONS ATTENDING THE OPERATIONS COMMITTEE MEETING

JAMAICA - COUNTRY STRATEGY PAPER

MONDAY, JULY 24, 1989 AT 11:30 A.M. IN ROOM E-1243

Committee Members

Messrs.	A. Karaosmanoglu	- Chairman
	S. Husain	- LACVP
	E. Jaycox	- AFRVP
	A. Stoutjesdijk	- EMNVP
	J. Linn	- DECVP
	D. Goldberg	- LEGVP
	J. Wood	- FPRVP
	H. Vergin	- OPNSV

Other Attendees

Messrs. A. Ray (EAS)
N. Roger (LACVP)
P. Loh (LA3DR)
M. Garcia-Zamor (LA3DR)
J. Sokol (LA3C2)
C. Delvoie (LA3C2)
H. Fazel (LA3C2)
J. Page (LA3TF)
F. Earwaker (SPR)
D. Hanna (FRS)
W. Sung (DFS)

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: July 18, 1989

TO: Operations Committee

FROM: Vinod Dubey, Director, EAS

EXTENSION: 78051/2

SUBJECT: JAMAICA: Country Strategy Paper Update - Agenda

1. The Operations Committee will meet on Monday, July 24, 1989 at 11:30 a.m. in Room E-1243 to discuss the CSP Update for Jamaica.

2. The last time the Committee met to discuss a country strategy paper for Jamaica was July 29, 1987. At that time we had just resumed quick-disbursing policy loans following a 15-month IMF stand-by arrangement. We could detect a turn-around in the economy after its dismal performance during the first half of the decade. Since then the overall growth performance has been reasonable despite a severe hurricane last September. The elections are over, and Mr. Manley has begun his second innings. Like Estenssoro's second term in Bolivia, and more recently Perez's in Venezuela, present indications are that Mr. Manley's second term will be the opposite of his first. With the next CSP at least a year away from now, this is an appropriate time to recheck our basic strategy and deliberate upon the points of emphasis in developing our approach to the new administration.

Issues

3. The Bank made three SALs between 1980 and 1985, and two more policy-based loans in 1987 to support improvements in public enterprise operations and trade and financial reforms. Two new policy-based loans in agriculture and in trade/finance are in process, and the eighth and final one, for supporting public sector reforms, is scheduled for FY92. Despite this prolonged period of adjustment, the CSP Update stresses that the adjustment program is far from over (para. 39), and highlights some issues (para. 22). The Region might comment upon the major achievements of the adjustment program thus far and comment on the key items of unfinished business. The Committee might wish to discuss in particular:

- the extent to which a sound system of fiscal management is in place. The large rise in the overall public deficit from 5.4% in 1987/88 to 13.3% in 1988/89 may have been largely due to the post-hurricane reconstruction program, but nonetheless issues remain on the rationalization of revenues (especially the delays in implementing the general consumption tax which would be a first step towards a value-added tax system), controls on and selection of public capital and recurrent expenditures, and the pricing policies and internal efficiencies of the major public enterprises such as the Jamaica Commodity Trading Company, the National Water Company, the electricity company, and the Petroleum Corporation of Jamaica;

- the structural transformation of the economy away from dependence on a few traditional exports and tourism. The promotion of non-traditional exports seem to be running into trouble. What has been the experience with exports of textiles and other free-zone items; what happened to our idea of expanding free-zones; what export strategies are being proposed and how can they be supported by our lending program?

- the exchange rate regime and its consistency with fiscal/monetary policy. The Jamaican Government has not thus far bought the idea of flexibility in exchange rates; the authorities want to maintain the arrangement for allocating foreign exchange through a Dutch auction system. Since late 1985, the Jamaican dollar had been effectively pegged to the U.S. dollar at J$5.5:1 by allocating sufficient foreign exchange to the auction. Maintenance of this exchange rate has recently exceeded the amount the Bank of Jamaica can deliver without incurring delays. Auction arrears had emerged. The real exchange rate has been appreciating during the last nine months. Is the current exchange rate viable, and, perhaps more importantly, is the system a satisfactory one given the potential need for abrupt and large devaluations? Does the reliance on fiscal and monetary policy to defend a fixed exchange rate constrain growth and contribute to the high unemployment rates?

- priorities of the sectoral policy agenda, especially in the trade and financial sectors and in agriculture. The Initiating Memorandum on the Agriculture SECAL was reviewed by the OC on November 18, 1988. Since then, the Region has encountered problems in reaching agreements with both the previous and the new administrations on key policy conditionalities, particularly on trade protection for small farmers, liberalization of interest rates on directed credit, programs to phase out generalized food subsidies, and further liberalization of export marketing organizations. What is the present status of these discussions and are we going to have this loan? What are the key changes that the Region envisages regarding financial policies, the pace of trade reforms, the monopoly powers of the JCTC, and the elimination of subsidies on rice, wheat, edible oils, skimmed milk, dried fish, fertilizers and private automobiles? Even when subsidies are reduced, will domestic prices be linked to world prices so that exchange rate depreciations and/or world price increases are passed on, or are domestic prices still going to be delinked?

4. Jamaica remains a highly-indebted high-risk country which is particularly vulnerable to term-of-trade changes. Its creditworthiness will remain contingent on progress on a satisfactory medium-term program, and the Bank's exposure will need to be closely monitored. The Region might elaborate upon the downside risks associated with the estimated financing gaps and on the prospects for equitable burden-sharing. Given the Fund's exposure in Jamaica (SDR329 million, 226% of quota at end-May 1989), how confident is the Region that the annual financing gaps (US$90-100 million) identified in the CSP (paragraph 32) could be managed with new

Fund programs and further reschedulings? What is the current stance of other creditors--specifically the U.S. and the IDB--regarding balance of payments support to Jamaica? Has the Region considered a contingency plan in the event of external shocks that can occur easily, such as a fall in the prices of bauxite/alumina or an increase in oil import prices?

OC Members

Messrs. Qureshi, Husain, Jaycox, Karaosmanoglu, Thalwitz, Rajagopalan
Fischer, Shihata, Wood, Vergin.

cc: Messrs. Lee (COD); Shakow, Liebenthal (SPR); Holsen (CEC); Rao, Steer (FRS); Burmester/Thahane (SEC); Baudon (OPNSV); Hopper (PPRSV); Bock (DFS); Goldberg (LEGOP); Kavalsky (FRM); Parmar (CIO); Pfeffermann (CEI); Baneth (IEC); Robless (OPNSV); (Ms.) Haug, Tanaka (EXC); Aguirre-Sacasa (EXT); Barandiaran (LACVP); Loh, Flood, Sokol, Fazel, LA3C2.

ARay:vlw

July 21,1989

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THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: July 17, 1989

TO: Operations Committee

FROM: Vinod Dubey, Director, EAS

EXTENSION: 78051

SUBJECT: Malawi: Country Strategy Paper (CSP) - Agenda

The Region has distributed the Malawi Country Strategy Paper to the members of the Operations Committee on June 20, 1989. The Committee will meet on Friday, July 21, 1989 in Room E1243 at 11:30 a.m. to consider the CSP.

Background

Since 1981, Malawi has implemented a structural adjustment program supported by three SALs extended by the Bank and three standbys by the Fund. In 1988 the IMF extended an ESAF while an Industrial Trade Policy Adjustment Credit was extended by the Bank. Despite these programs Malawi's economic performance was weak. Per capita income and consumption has continued to decline and the country has suffered bouts of large current account deficits and high inflation. The short run adjustment problems have been caused by a combination of domestic policy failure exacerbated by external shocks in the form of adverse terms of trade, droughts and security problems connected with civil strife in Mozambique.

While the adjustment efforts may have ameliorated an even worse outcome, Malawi's development challenge remains formidable. Low productivity combined with high population growth, pervasive poverty even by Sub-Saharan African country standards, inadequate human resource development and the threat of environmental degradation add up to a long term development challenge of multi-dimensions.

The Committee may wish to raise the following issues in regard to the different elements and implications of country strategy. These issues are: agriculture as a source of growth, poverty reduction and related human resources development issues, macroeconomic stances and public expenditures, and the macroeconomic projections and the policy framework.

Agriculture as a Source of Growth

The CSP identifies agriculture as the main source of growth in the medium term. Small holder agricultural productivity is to be the primary focus for restoring growth. This strategy supports the poverty alleviation objective very well.

The Region may be asked to describe the policy instruments to be used to raise agricultural productivity and the capacity of the various institutions in the sector to implement this strategy.

The Region may wish to comment on the priorities within the agricultural sector, to ensure the proper phasing of output growth from both the estate and small holders to meet overall growth targets.

Poverty Reduction and Human Resources Development

The CSP documents the Malawi government's increased concern for equity and distributional issues. Poverty reduction issues are intimately linked to the human resource development strategy to raise productivity and earning capacity.

The Region may wish to comment on the priorities for Bank's strategy in the social sectors: population, education and health and the policy environment for human resources development given the relative neglect of these sectors by the Government in the past.

The Region may wish to comment on the proposed Structural Adjustment Loan (SAL IV) as a principal instrument to provide a medium term policy framework to address poverty reduction.

Macroeconomic Stances and Public Expenditures

The CSP articulates the concern that stringent macroeconomic stances intended to control inflation and reduce current account deficits, may limit the availability of financial resources for essential public expenditures and for the private sector to take advantage of the improving policy environment. The IMF and the Government favor tight fiscal-monetary policies with less frequent exchange rate adjustments while the Bank prefers less stringent fiscal-monetary measures with more frequent exchange rate adjustments.

The Region may wish to describe its position regarding the extent of the trade off between reducing absorption and devaluing the currency in Malawi and the implications of the trade-off for transition of the macroeconomy towards reduced inflation and current account deficits.

The Region may wish to comment on the priorities for expenditure expansion in areas which have received inadequate funds in the past and the areas in which expenditure cuts are consistent with macroeconomic stability and are also in line with the composition of foreign assistance.

Macroeconomic Projections and the Policy Framework

The CSP provides a base case scenario and three alternative scenarios that are related to external shocks, domestic policy slippage and underfunding of the adjustment program.

The Region may wish to comment on the output growth projected in the base case and the policy measures consistent with it. In particular, the Region may describe the basis for the the near 5% per year agricultural output growth and even higher agricultural export growth and the prospects for the growth in manufactures exports.

The Region may wish to comment whether Malawi would take recourse to microeconomic controls in the face of future external shocks and the extent of the risk associated with the combination of an external shock with domestic policy slippage.

Operations Committee Members

Messrs. Qureshi, Husain, Jaycox, Karaosmanoglu, Thalwitz, Rajagopalan, Fischer, Shihata, Wood, Vergin

cc: Messrs. Lee (COD);Shakow, Liebenthal (SPRPA); Holsen (CEC); Rao, Steer (FRS); Burmester/Thahane (SEC); Baudon (OPNSV); Hopper (PPRSV); Bock (DFS); Goldberg (LEGOP); Kavalsky (FRM); Parmar (CIO); Pfeffermann (CEI); Baneth (IEC); Robless (OPNSV); Ms. Haug, Tanaka (EXC); Agarwala (AFRCE); Aguirre-Sacasa (EXT); O'Brien (AFRCE); Sandstrom (AF6DR); Messenger, Nkojo, King (AF6CO); Ali (AF6AG)

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THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

89071800 9 2

DATE: July 17, 1989

TO: The Operations Committee

FROM: Vinod Dubey, Director, EAS

EXTENSION: 78051

SUBJECT: Tanzania: Country Strategy Paper (CSP) - Agenda

The Tanzania Country Strategy Paper was distributed to the members of the Operations Committee on June 13, 1989. The Committee will meet on Friday, July 21, 1989 in Room E1243 at 10:30 a.m. to consider the CSP.

Background

After nearly two decades of pursuing socialist and self reliance ideals, Tanzania began to change its economic course in the late 1980s.

The Economic Recovery Program (ERP) that was introduced in mid 1986 with Bank and Fund support, took a comprehensive approach to reform. The ERP included substantial exchange rate adjustments, a refurbished export retention scheme, raising of real interest rates to positive levels, controlling public sector borrowing and reducing a large number of price controls. The ERP was supported by the IDA Multisector Rehabilitation Credit (MRC) of $165 million in late 1986 and a Fund standby arrangement. External assistance began to play a prominent part in financing large current account deficits that had emerged.

These policy and institutional reforms introduced under the ERP and increased external assistance led to substantial improvement in economic performance. Per capita income increased for the first time since 1980, manufactures and traditional exports rose rapidly, per capita food availability and consumer goods increased, contributing to the improved well being of the population. However, the reform program is by no means complete and a substantial unfinished agenda exist to lay the basis for medium and long term growth. This agenda comprises both short run macroeconomic measures as well as structural reforms. The recovery program was less successful in the monetary area with inflation persisting at 25-30% per year, the exchange rate regime needs to provide continuing incentives for tradable goods production, while domestic marketing of agricultural products remain problematical. Long term development issues relating to human resources, poverty alleviation and the environment pose a formidable part of the unfinished agenda for both policy and institutional reforms.

The Committee may wish to take up the following issues in discussing the CSP (a) the pace of reforms, (b) macroeconomic stability and the exchange rate regime, (c) incentive structure reforms, (d) the size and composition of Bank lending programs.

(a) The Pace of Reform

The CSP describes the pace of reform as a central issue for the success of the recovery program to lay the basis for medium and long term development.

> The Region may wish to comment on the pace of reform given that there is an important segment of the Tanzanian society that is suspicious of reforms intended to give a greater role to the market.

> The Region may also comment on the credibility of the reforms to private sector agents who may take advantage of short run price movements while eschewing long run commitment via investment. How is this commitment to be assured?

(b) Macroeconomic Stability and the Exchange Rate Regime

Even though public sector deficits have been reduced, monetary aggregates have grown significantly with inflation rates remaining around 25-30% per year.

> The Region may wish to describe the nature of a short run policy framework needed for financial stability while providing sufficient funds to the private sector to take advantage of the improving incentives.

> The Region may wish to describe an exchange rate regime that could be put in place to ensure that sufficient and continuing incentives are provided to the tradable sectors consistent with the substantial foreign capital inflows that are indicated by the projected current account deficits in the balance of payments.

(c) Incentive Structure Reforms

Even though the reforms to date signify a fundamental departure from earlier policies, some incentive reforms assume strategic importance for increased efficiency.

> The Region may wish to comment on the needed reforms in agricultural marketing, focussing on the transition to a free system, given the present practises of mandated procurement of crops, cost plus basis for reimbursement of funds to cooperatives for crop procurement and the continuing monopsonistic presence of marketing boards.

> The Region may also wish to comment on future pricing policies of public enterprises given that their present losses contribute to a large drain on the government's budget.

(d) Size and Composition of the Banks Lending Programs

The proposed Bank assistance strategy comprises a number of elements; to help improve economic management and resource allocation; reduce and rationalize the role of the public sector; reduce sectoral and physical constraints; develop entrepreneurship, address sectoral and longer term issues and, help mobilize adequate external resources.

The Region may wish to describe the priorities in its assistance strategy given a diversified effort to address both short run and longer term issues.

The Region may wish to comment on the size of the Bank's lending program, in relation to other donors and the rationale for fast disbursing adjustment loans of 60% of Bank total lending, where many of the issues to be addressed in agriculture, social sectors and in institutional building in general appear to be of a long term nature.

Operations Committee Members:

Messrs. Qureshi, Husain, Jaycox, Karaosmanoglu, Thalwitz, Rajagopalan, Fischer, Shihata, Wood, Vergin

cc: Messrs. Lee (COD); Shakow, Liebenthal (SPR), Holsen (CEC); Rao, Steer (FRS); Burmester/Thahane (SEC); Baudon (OPNSV); Hopper (PPRSV); Bock (DFS); Goldberg (LEGOP); Kavalsky (FRM); Parmar (CIO); Pfeffermann (CEI); Baneth (IEC); Robless (OPNSV); Ms. Haug, Tanaka (EXC); Agarwala (AFRCE); Aguirre-Sacasa (EXT); O'Brien (AFRCE); Sandstrom (AF6DR), Messenger, Nkojo, King (AF6CO); Ali (F6AG)

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THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: July 11, 1989

TO: Operations Committee

FROM: A. Ray, Acting Director, EAS

EXTENSION: 78057

SUBJECT: TANZANIA: CSP and MALAWI: CSP

The Operations Committee will meet on Friday, July 21, 1989 in Room E-1243 to consider the TANZANIA: Country Strategy Paper (at 10.30 a.m.) and the MALAWI: Country Strategy Paper (at 11.30 a.m.). The agendas for the meetings will be issued shortly. The meetings will be chaired by Mr. A. Karaosmanoglu.

Operations Committee

Messrs. Qureshi, Husain, Jaycox, Karaosmanoglu, Thalwitz, Rajagopalan, Fischer, Shihata, Wood, Vergin

cc: Messrs. Lee, Shakow, Holsen, Rao, Burmester/Thahane, Liebenthal, Steer, Baudon, Hopper, Bock, Goldberg, Kavalsky, Parmar, Pfeffermann, Baneth, Robless, Ms. Haug, Tanaka, Agarwala Aguirre-Sacasa, O'Brien, Sandstrom, Messenger, Ali, Nkojo, King

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July 20, 1989

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

890719001

(postponed)

DATE: July 18, 1989

TO: Operations Committee

FROM: Vinod Dubey, Director, EAS

EXTENSION: 78051

SUBJECT: YUGOSLAVIA: Proposed $300 million SAL II Green Cover Package - Agenda

1. The Operations Committee will meet on Thursday July 20, at 2.30 p.m. in Room E-1243, to consider the Green Cover Package for a proposed Second Structural Adjustment Loan to Yugoslavia in the amount of $300 million. The Committee had discussed the Initiating Memorandum for this operation in June 1988. Concern then centered on stabilization, enterprise reform and the credibility of the reforms. Against a background of inflation of 160% in 1987, the Region said at the June 1988 meeting of the OC that there were reasons to believe that the Government was that time serious about the reforms. Now, a year later, and with inflation "spiralling" at 600% a year, the Region is requesting that the operation be negotiated.

Background

2. The Region candidly describes the unsatisfactory implementation of SAL I (FY83) and the backsliding of reforms after the loan had been completely disbursed. In his cover memorandum, Mr. Lari stresses that "the evidence is there now" for the Government's seriousness over the reforms, although the short-run political and economic setting remains uncertain. The role of the Fund in Yugoslavia is not clear, and it is difficult to see how the Fund-supported program which would begin in September 1989, will succeed where previous programs had failed. The Fund Board is expected to consider an 18-month Stand-by in September, with a "mid-term" review taking place by end-1989 (i.e. three months later).

Risks of the Operation

3. The President's Report is silent on the risks of the operation, but these receive full attention in the cover memorandum which identifies (a) the possibility of sluggish supply response to the reforms; (b) the persistence of inflationary pressures; and (c) the cost of adjustment being too onerous for the program to continue. All the cover memorandum promises about inflation is that the program "should prove effective in moderating the acceleration of inflation over the next six months..." Besides these risks there are also political and ethnic tensions. Bank exposure is not likely to exceed financial guidelines owing largely to reduced lending during the past few years.

- Does the OC consider that the benefits from this operation would exceed the risks?

- Even if exposure is not a consideration, would it be prudent to raise lending when there are so many uncertainties?

- Would it be preferable to delay this operation until the Fund had conducted its "mid-term" review by end-1989?

Inflation and the Macroeconomy

4. The record of inflation has been alarming, and despite a series of IMF-supported programs, it appears to be accelerating. Based on the draft President's Report annual inflation rates increased from 20% in the 1970s to 50% in 1980-85, and accelerated to 88% in 1986 and further to 167% in 1987. In the first four months of 1988, annual inflation was 90% (para. 9), before a Fund Stand-by was put in place in May 1988. By the end of the year inflation had averaged "over 250%" in 1988 (para. 12). Inflation seems now to be proceeding at considerably higher rates.

- The Region may wish to explain how inflation got out of hand under successive stabilization programs, and whether the National Bank of Yugoslavia is now in a position to contain monetary expansion. Would not the same factors as before, including the autonomy of the enterprises and the decentralization of system, again militate against effective control of the money supply?

- Can the Region clarify the impact of the high inflation on the real economy, in terms of inter-regional and interpersonal income distribution, savings and the financing of investment, the shifts of income between the domestic and foreign sectors, and offer a projection of future inflation rates?

- While inflation lasts, would it at all be possible to eliminate from the economy the "financial indiscipline" the Region repeatedly mentions?

- How can real interest rates be set at 15% (para. 20) in conditions of high inflation?

Trade Liberalization

5. The foreign exchange allocation system having been liberalized, trade is said to be effectively constrained by the trade regime. On the side of imports, tariffs are not high, but protection is afforded by restrictive administrative controls which classify imports into control categories. The Government seems to have reduced tariffs "on more than a thousand items at the beginning of 1989" (para. 35), but temporary assistance would be given to local producers who suffer from reduced protection after a study is concluded (ibid.). On administered import categories, liberalization takes the form of moving items from more restricted to less restricted categories (para. 34). In para. 32 a statement reads "The Government now intends to remove many controls and reduce others in order to generate the competitive pressures needed..." The policy matrix shows liberalization undertakings only in respect of import category LB (the free list): share of imports on that list would increase from 11% to 65% (it is not clear of what) by June 1989. Liberalization affecting other categories seems to require prior study and is yet to be agreed.

- The Region might clarify the liberalization program summarized in the matrix, the degree of Government commitment on liberalization, and whether liberalization can be expected to proceed unhampered by the prevailing unstable economic conditions.

Financial Restructuring

6. A set of financial restructuring provisions is shown in the policy matrix. The program seeks to strengthen the legal framework, bolster NBY's supervisory and regulatory powers, ensure proper bank auditing and restructuring the banking system. Five of twenty major problem enterprises are to be liquidated or rehabilitated by the second tranche, with a program to be agreed on rehabilitating or restructuring enterprises facing difficulties. Financial restructuring will be further pursued under a projected Financial Sector Adjustment Loan in 1990/91 which will be part of a series of further adjustment operations and a larger lending program.

- Considering that stabilization is not yet in hand, how much success can be expected of the financial reforms?

- Can the financial reforms over the medium term be indicated more systematically so that the proposed program of structural reform under SAL II is seen as part of a more comprehensive medium-term plan?

Economic Projections

- Why are ICORs projected to remain at 8 until the late 1990s?

- Are the projected long-term capital inflows realistic?

Distribution:

Messrs. Qureshi, OPNSV (o/r); Karaosmanoglu, ASIVP; Husain, LACVP; Jaycox, AFRVP; Thalwitz, EMNVP; Rajagopalan, PREVP; Fischer, DECVP; Wood, FPRVP; Shihata, LEGVP; Vergin, OPNSV.

cc: Messrs. Lee, COD; Shakow, SPR; Holsen, CEC; Rao, FRS; Burmester/ Thahane, SEC; Liebenthal, SPRPA; Steer, FRS; Baudon, OPNSV; Hopper, PPRSV; Bock, DFS; Goldberg, LEGOP; Kavalsky, FRM; Parmar, IFC (CIO); Pfeffermann, IFC (CEI); Baneth, IEC; Robless, OPNSV; Ms. Haug, EXC; Tanaka, EXC; Lari, EM4DR; Hasan, EMNVP; El Maaroufi, EMNVP; Nouvel, EM4CO.

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THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: July 19, 1989

TO: Operations Committee

FROM: Randolph L.P. Harris, RLH Acting Director, COD

EXTENSION: 73353

SUBJECT: **BRAZIL - Rondonia Natural Resources Management Project Cancellation of OC Meeting**

The OC meeting scheduled for Thursday, July 20, at 3:30 p.m., has now been cancelled. In his memo to Mr. Husain of July 10, 1989 (which was in the package distributed to you on July 13), Mr. Qureshi called for an OC meeting contingent upon AGR and ENV confirming "from a technical viewpoint that reforestation with coffee and cocoa is the only suitable approach to take in the circumstances." As no such confirmation has been received, Mr. Karaosmanoglu has decided to cancel the meeting.

Distribution:

Messrs. Qureshi (o/r) (OPNSV); Husain (LACVP); Jaycox (AFRVP); Karaosmanoglu (ASIVP); Thalwitz (EMNVP); Rajagopalan (PREVP); Fischer (DECVP); Shihata (LEGVP); Wood (FPRVP); Vergin (OPNSV)

cc: Messrs. Lee (o/r) (COD); Dubey (EAS); Shakow (SPR); Holsen (CEC); Rao (FRS); Burmester/Thahane (SEC); Liebenthal (SPRPA); Steer (FRS); Baudon (OPNSV)

For Information:

Messrs. Hopper (PPRSV); Bock (DFS); Goldberg (LEGOP); Kavalsky (FRM); Parmar (CIO); Pfeffermann (CEI); Baneth (IEC); Robless (OPNSV); Tanaka (EXC); Choksi (o/r) (LA1DR); Goodland (LATEN); Coirolo (LA1AG); Petit (AGRDR); Warford (ENVDR); Duncan, Akiyama (IECCM); Casley, Srinivasan (COD)

Mmes. Haug (EXC); Birdsall (LA1PH); Pomerantz (LA1AG)

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Steve/PC#6/AG6

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

OC Did not take place

RECEIVED
ASIVP JUL 19 1989

DATE: July 18, 1989

TO: Operations Committee

FROM: Randolph L.P. Harris, Acting Director, COD RLH

EXTENSION: 73353

SUBJECT: BRAZIL - Rondonia Natural Resources Management Project Agenda

1. The Operations Committee (OC) will meet on Thursday, July 20, at 3:30 P.M. in Room E-1243 to discuss the Brazil Rondonia Natural Resources Management Project, for which a $150 million loan is proposed. The following is suggested as an agenda for the meeting:

Background

2. The proposed Rondonia project would, through credit and extension to some 50,000 poor farmers (with average per capita income of below $200), expand Brazil's cocoa production by the year 2000 by about 5.6% (28,600 tons) and its coffee production by about 1.9% (40,000 tons). This would be by far the largest expansion of these crops financed by the Bank since restrictions were imposed in 1982.[1] Because coffee and cocoa (a) are produced solely by Part II countries and consumed primarily in Part I countries, and (b) face relatively price- and income-inelastic demand, the Bank normally does not lend for expansion of coffee or cocoa production, except in countries without alternatives. The recent draft PPR paper, "Bank Policy on the Financing of Primary Commodities," recommends relaxing this policy, but only for IDA countries, which have fewer alternative sources of finance and, as a group, have been losing market share to IBRD countries. As this project would not meet existing or proposed guidelines for Bank financing of coffee or cocoa, the Region has requested an exception, on environmental grounds.

Special Importance of the Project

3. The Region considers this project particularly important, because (a) it would be the model for applying agro-ecological zoning and related policy reforms to other provinces in the Amazon basin, (b) the Amazon is perhaps the single greatest focus of environmental attention in the world, (c) the Bank has special responsibility for helping solve Rondonia's

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1/ From 1983-87, 10 cocoa projects with combined incremental production of 32,700 tons, and 19 coffee projects with combined incremental production of 60,800 tons were approved, mostly in IDA countries.

environmental problems because of the adverse impact of our earlier road financing there, and (d) our environmental credibility with both the Government of Brazil and outside institutions could be affected. The OC may wish to consider whether the proposed project is indeed of such special environmental importance that exceptions to Bank commodities policy might be justified.

Benefits from Coffee and Cocoa Planting

4. The Region considers planting of perennial crops (on already cleared land) essential for carrying out the basic environmental strategy of the project, which is to restrict development to areas with sustainable agricultural potential (as demarcated by a major agro-ecological zoning exercise), and retain the forest cover elsewhere. Because annual crops quickly deplete the soil, farmers have been abandoning cleared lands within a few years, and moving on to "slash and burn" additional forest areas, either legally (within their allocated 35 ha plots), or illegally. With suitable perennial crops, however, the land can remain productive indefinitely, and the farmers, given their limited labor supply, will no longer have the incentive or resources to keep clearing new areas. The Region might be asked to give some quantitative estimates of (a) the forest hectarage (in both the agriculture and the forest zones) that would be preserved due to coffee and cocoa planting under the project, (b) the economic value of preserving a hectare of forest, and (c) the net benefits to the farmers from each hectare of coffee and cocoa, as compared to alternative crops. The OC may wish to consider (a) whether this strategy will indeed substantially reduce forest destruction, and (b) whether there are any environmentally and economically viable alternatives to coffee and cocoa (e.g., tree plantations or other perennial crops).

Need for Bank Finance of Coffee and Cocoa

5. The Region believes it could not proceed with this project if the Bank would not finance the credit and extension components for coffee and cocoa, because (a) these are the largest project components, together accounting for one-third of project cost, (b) these components are the essential "production leg" to balance the "conservation leg" and make the entire project palatable to Brazil, and (c) Bank finance for these components is critical both for their success and for the Bank's environmental credibility in Brazil. The OC may wish to consider whether these arguments are persuasive. (In the Malaysia - Sabah Land Settlement and Environmental Management Project, the Bank financed the foreign exchange cost excluding that for the cocoa component.)

?

Impact on Other Coffee and Cocoa Producers

6. The Commodities Division (IECCM) (memo attached) has estimated that this project would have an adverse price impact of about 3-4% for cocoa[2] and 1.3% for coffee by the year 2000, which would reduce the annual

2/ The 5.4% in the attached memorandum assumes that producer prices in Cote d'Ivoire and Ghana remain fixed so there are no output declines there.

export revenue of other Part II countries by some $200-250 million per year. Coffee and cocoa importing countries, primarily Part I, would, of course, have roughly offsetting gains. As for Brazil itself, its annual incremental export revenue would be only about $36M for coffee ($82M from the incremental output, less $46M from the price reduction to other Brazilian producers) and $10-15M for cocoa ($33M less $18-23M). The OC may wish to consider (a) whether the cost to other Part II countries, especially the poorer ones in Africa, would be too great to go ahead with the project as designed, and (b) whether the recent collapse of the International Coffee Agreement, and recent declines in coffee and cocoa prices, makes this a particularly inopportune time to finance these crops.

Possibility of Offsetting Production Decreases Elsewhere in Brazil

7. Given the expected benefits to Brazil of this project, but the adverse impact on other coffee and cocoa exporters, a solution might be to have Brazil take steps to reduce production by an equal amount elsewhere in the country, either by changing incentives (e.g., through export tax increases) or by more direct measures. The OC might consider the feasibility of obtaining such a commitment from Brazil, either as part of this project or through our broader sector dialogue, and how this could best be approached.

Precedent for Rest of Amazon and Other Countries

8. This might be the first project in which the Bank agreed to an exception on environmental grounds to its commodities policy.[3] As such, it would set a precedent both for other provinces in the Amazon basin, and for other countries. The OC might consider (a) how well-founded is the Region's view that there would not be similar large areas in other Amazon provinces where coffee or cocoa would be the preferred crop, and (b) whether a similar environmental case could be made for financing coffee or cocoa in many other countries, and if so, whether this would effectively undermine Bank commodities policy.

Attachment

3/ The environment was a secondary factor in a recent exception for coffee production in Laos. The argument there was that coffee was the best alternative to timber (from the rainforest) as a source of foreign exchange.

Distribution:

Messrs. Qureshi (o/r) (OPNSV); Husain (LACVP); Jaycox (AFRVP); Karaosmanoglu (ASIVP); Thalwitz (EMNVP); Rajagopalan (PREVP); Fischer (DECVP); Shihata (LEGVP); Wood (FPRVP); Vergin (OPNSV)

cc: Messrs. Lee (o/r) (COD); Dubey (EAS); Shakow (SPR); Holsen (CEC); Rao (FRS); Burmester/Thahane (SEC); Liebenthal (SPRPA); Steer (FRS); Baudon (OPNSV)

For Information:

Messrs. Hopper (PPRSV); Bock (DFS); Goldberg (LEGOP); Kavalsky (FRM); Parmar (CIO); Pfeffermann (CEI); Baneth (IEC); Robless (OPNSV); Tanaka (EXC); Choksi (o/r) (LA1DR); Goodland (LATEN); Coirolo (LA1AG); Petit (AGRDR); Warford (ENVDR); Duncan, Akiyama (IECCM); Casley, Srinivasan (COD)

Mmes. Haug (EXC); Birdsall (LA1PH); Pomerantz (LA1AG)

THE WORLD BANK INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

Date: July 18, 1989

To: Mr. S.J. Ettinger, CODOP

From: T. Akiyama and P. Varangis, IECCM.

Subject: Estimated Effects of the Rondonia Natural Resource Management Project on World Coffee and Cocoa Prices and on Export Revenues of Selected Countries

1. As requested, we have estimated the effects of the above project on world coffee and cocoa prices and on export revenues of selected countries and regions using our global econometric models of the two commodities. We ran the models up to the year 2000.

2. Coffee. We assumed for this exercise that the global export quota system of the International Coffee Agreement would be suspended during the period of simulation. Changes in the main variables caused by the project are given in Table 1. As the incremental production from the project increases with time, the effects are found to be minimal in the first half of the 1990s and to increase with time. As shown in Table 1, the price impacts are estimated to be 0.8% in 1995 and increase to 1.3% in 2000. World real export revenues would be reduced by 0.5% in 1995 and 0.8% in 2000.

3. It is to be noted that the incremental coffee production from the project by the year 2000 is much closer to 2% of total Brazilian production than the 1% mentioned in Mr. Husain's memo to Mr. Qureshi of June 28 (para. 7).

4. Cocoa. The results of our model simulations are shown in Table 2. They indicate that with the project, world prices are estimated to be lowered by 1.5% in 1995 and by 5.4% in 2000. World real export revenues are projected to be reduced by 0.9% in 1995 and by 4.7% in 2000.

Attachments

TAkiyama:akw

c.c. Mr. Duncan, IECCM

Table 2: Cocoa: Changes in World Prices and Real Export Revenu of Selected Countries / Regions

	1995	1997	2000
World Price (%)	-1.5	-3.3	-5.4
Value of Production			
World (millions 1987 US$)	-21.1	-73.6	-173.7
(%)	-0.9	-2.6	-4.7
Brazil (millions 1987 US$)	3.3	2.7	1.4
(%)	0.9	0.6	0.2
Cote d' Ivoire (millions 1987 US$)	-11.4	-29.8	-63.3
(%)	-1.5	-3.3	-5.4
Ghana (millions of 1987 US$)	-4.0	-10.6	-22.7
(%)	-1.5	-3.3	-5.4
Malaysia (millions of 1987 US$)	-4.5	-12.8	-26.5
(%)	-1.5	-3.4	-5.6
eria (millions of 1987 US$)	-2.1	-6.1	-12.9
(%)	-1.5	-3.6	-6.1

Note: World includes Brazil

Table 1: Coffee: Changes in World Prices and Export R
of Selected Countries / Regions

	1995	1997	2000
World Price (%)	-0.8	-1.3	-1.3
Export Revenues			
World (mill. 1987 US$)	-59.3	-100.1	-107.5
(%)	-0.5	-0.8	-0.8
Brazil (mill. 1987 US$)	15.9	23.5	35.9
(%)	0.5	0.7	1
Rest of South America (mill. 1987 US$)	-23.0	-39.8	-44.4
(%)	-0.9	-1.5	-1.6
Central America (mill. 1987 US$)	-14.5	-26.6	-28.1
(%)	-0.8	-1.4	-1.4
Africa (mill. 1987 US$)	-22.1	-40.9	-44.2
(%)	-0.8	-1.4	-1.4
Asia (mill. 1987 US$)	-12.8	-23.0	-27.9
(%)	-0.9	-1.5	-1.6

Note: World includes Brazil

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

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OFFICE MEMORANDUM

DATE: July 13, 1989

TO: Operations Committee

FROM: Ducksoo Lee, CODDR

EXTENSION: 73348

SUBJECT: **BRAZIL - Rondonia Natural Resources Management Project Notice of Operations Committee Meeting**

A meeting to discuss the above project will take place on Thursday, July 20 at 3:30 P.M. in Room E-1243. The main issue is whether, on environmental grounds, an exception should be made to the Bank's policy on financing of coffee and cocoa. Attached are the following background documents:

(a) Mr. Qureshi's response to Mr. Husain, dated July 10, 1989;

(b) Mr. Husain's memo to Mr. Qureshi, dated June 28, 1989, asking for an exception to the Bank's commodities policy;

(c) Mr. Akiyama's memo to Mr. Choksi, dated February 7, 1989, on the commodities issue;

(d) Mr. Lee's comments on the FEPS, on Mr. Qureshi's behalf, to Mr. Steckhan, dated December 30, 1988; and

(e) the FEPS, with a covering note from Ms. Pomerantz to Mr. Husain, dated December 8, 1988;

An agenda for the meeting will be issued shortly.

Attachments

Distribution:

Messrs. Qureshi (OPNSV); Husain (LACVP); Jaycox (AFRVP); Karaosmanoglu (ASIVP); Thalwitz (EMNVP); Rajagopalan (PREVP); Fischer (DECVP); Shihata (LEGVP); Wood (FPRVP); Vergin (OPNSV)

cc: Messrs. Dubey (EAS); Shakow (SPR); Holsen (CEC); Rao (FRS); Burmester/Thahane (SEC); Liebenthal (SPRPA); Steer (FRS); Baudon (OPNSV)

For Information:

Messrs. Hopper (PPRSV); Bock (DFS); Goldberg (LEGOP); Kavalsky (FRM); Parmar (CIO); Pfeffermann (CEI); Baneth (IEC); Robless (OPNSV); Tanaka (EXC); Harris, Casley, Srinivasan (COD)

Ms. Haug

SEttinger:mda
Steve/PC#6/AG6
14-JUL-89/ 9:10:00

The World Bank
Washington, D.C. 20433
U.S.A.

MOEEN A. QURESHI
Senior Vice President, Operations

Mr Harris
Draw
July 10

July 10, 1989

Mr. Husain:

I have read this carefully but I have difficulty in fully comprehending the strategy that is set out in your note. It appears to rest on the following premise:

The earlier "Polonoroeste" strategy did not work because (i) the Government did not follow sound public/regulatory policies; and (ii) because perennial tree crop production was not established to replace forests.

Now it is stated that the Government is prepared to do (i) and we must help them do (ii) because without that, the plan does not work.

At the same time, I am informed that only limited areas in the Amazon are suitable for coffee and cocoa production so that this project will not become the forerunner of a major expansion in coffee and cocoa production in the Amazon Basin.

From the Bank's standpoint, three issues stand out:

First, we should not try to do something that is counter to a long-established and fairly sensitive policy unless the project is truly important and replicable on a large scale.

Second, if the project is replicable on a large scale, then we have got a pretty contentious issue on our hands in terms of policy. In this case we should first look into the overall implications of this issue -- and whether it is still defensible in a broader economic context.

Third, how certain are we that coffee and cocoa are the only perennial crops that can be grown in these areas.

This is a project that needs more careful institutional review, including review by the Operations Committee. However, before going to the Operations Committee I would like the Agriculture and Environment Departments in PPR to take a careful look at it and confirm from a technical viewpoint that reforestation with coffee and cocoa is the only suitable economic approach to take in the circumstances. On the basis that this judgement is supportive, we should then discuss this in the Operations Committee.

cc: Mr. Rajagopalan
Mr. Lee

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: June 28, 1989

TO: Mr. Moeen A. Qureshi

FROM: S. Shahid Husain

EXTENSION: 39001

SUBJECT: BRAZIL - Proposed Rondonia Natural Resource Management Project
Bank Financing of Coffee and Cocoa

1. I refer to Mr. Ducksoo Lee's memo of December 30, 1988, conveying your comments on the FEPS for this project, and to Mr. Akiyama's (IECCM) subsequent memo of February 7, 1989, regarding proposed Bank financing of coffee and cocoa production under the project.1/ The issues raised in Mr. Ducksoo Lee's memo have been discussed by staff of this Department and the COD, and appropriate guidance has been given to the appraisal mission. However, the question of Bank financing for coffee and cocoa has yet to be resolved. Since the productive strategy of the project is based almost entirely on these two perennial crops, a decision on this matter is required prior to authorizing the appraisal mission's departure.

2. It is now generally agreed that most of the problems of the first generation of Northwest Program ("POLONOROESTE") projects were due to two factors. First, during the design of the Program, inadequate attention was paid to the policy framework for development activities in the Amazon Basin. Much of the uneconomic agricultural investment and extensive deforestation in that region during the past two decades has been due to misguided public policies, regulations and investment programs (e.g., land registration and titling procedures which actively encouraged forest clearing, inappropriate forestry protection practices and regulations, special fiscal incentives and subsidized credit lines for unsustainable livestock production), which have either purposely or inadvertently been encouraging rapid depletion of the region's natural resource base. As a result, a situation has developed in which there are enormous contrasts between the costs to the country of a predatory form of development and the often high, albeit short-lived, financial gains to the private beneficiaries of these policies and programs.

3. The second major weakness of the Northwest Program has been its inability to successfully establish perennial treecrops in Rondonia. Since migrants have not been effectively assisted in planting such crops, they have continued instead to deforest ever increasing areas in order to plant

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1/ Appraisal, originally planned for February 1989, was delayed pending submission of this project to a new review process which the Ministries of Planning and Finance have adopted for all operations proposed for external financing. This step has now been completed and an official Government request to proceed with appraisal was received in the Bank last week.

annual crops. In order to cultivate annual crops, for all intents and purposes the farmers 'mine' the soils of their limited fertility for a few years. After that, they abandon them to livestock production, which further degrades the land, while the farmers move on to deforest new areas in order to begin the annual crop cycle all over again. The startling consequences of this small farmer "slash and burn" cultivation pattern, followed by large-scale livestock production, have been unmistakably recorded in satellite images which show that the cleared area in the Amazon Basin has increased from about 30,000 km2 in 1975 to almost 600,000 km2 in 1988 (i.e., from less than 1% to nearly one-sixth of the tropical forest). Nowhere has the situation been more dramatic than in the State of Rondonia, where about one-fourth of the forest has already been cleared.

4. The proposed Rondonia Natural Resource Management Project would, we believe, mark the beginning of a new stage in the Bank's involvement in the Northwest Program. The distinguishing feature of this project, largely missing from earlier agricultural operations in the Northwest, would be the explicit effort to introduce changes in the policy and regulatory framework (and its enforcement), in order to better support the long-term objectives of sound natural resource management. The project would also build on many of the important technical and institutional lessons learned in the course of implementation of the earlier generation of POLONOROESTE projects, and would benefit from the very marked changes in political awareness within Brazil itself and the growing commitment to confront the environmental problems of the Amazon.

5. Preparation of this project has involved, <u>inter alia</u>, a major agro-ecological zoning exercise for Rondonia, which has been supported by UNDP and FAO and has drawn the attention and support of numerous Government agencies and NGOs. Basically, the objective of the zoning exercise was to subdivide the State into different zones based on identifiable classes of land use potential, and then to derive appropriate development strategies for each identified zone. Overall, the State was divided into six zones, of which only one (Zone 1), where most of the forest cover has already been cleared, was identified as having the potential for sustainable cultivation; the other five zones would remain under forest cover. The resulting recommendations for Zone 1, which essentially includes the best areas of the State from an agricultural standpoint, are based on intercropping of perennial crops (principally cocoa and coffee) and agroforestry. From an environmental standpoint, any deviation from this strategy would be extremely detrimental to the State's natural resource base, with obvious and well understood consequences both for Brazil and the international community (climatic changes, loss of biodiversity, etc.).

6. We have made it a precondition of our involvement in the proposed operation that the Brazilian Government agree to a series of policy and regulatory reforms and enforcement measures designed to ensure that future direct and indirect Government interventions and private sector initiatives in Rondonia are channeled only into sustainable and environmentally sound economic activities, based on this agro-ecological zoning exercise. The nature of these reforms has been detailed in the letter dated April 29, 1988, from the Minister of Interior to Mr. Conable. In the interim, not only has progress been made in implementing various undertakings spelled out in the letter, but President Sarney has also announced a major environmental initiative to protect the Amazon area and has established high-level working groups to develop specific plans.

7. The Department is well aware of existing Bank policy which restricts the conditions under which the Bank will normally finance projects involving production of coffee and cocoa. Project staff have reviewed the details with IECCM and are in basic agreement on the numbers involved. In the case of cocoa, production would increase by about 28,600 tons by the end of this century (e.g., about 5% of Brazilian production). Moreover, presently only 7% of Rondonia's cocoa production is of exportable quality. If the project is successful, this figure may be raised to about 20% by 1997/98, meaning that some additional 5,000 tons of dry beans (or about 1% of Brazilian exports) would reach the world market. There has been a trend of annual decreases in marginal areas in Bahia, Brazil's main cocoa producing state, but it is not possible to guarantee that these would fully offset the increased production from Rondonia. With regard to coffee, production would increase by about 40,000 tons (equivalent to about 1% of total Brazilian production).

8. IECCM has given project staff guidance concerning marginal revenues to use in calculating the economic viability of the project. Using this methodology, preliminary estimates indicate that the project is likely to have an ERR of no less than 13%, with the financial rate of return to individual farmers being, of course, much higher (20% - 50%). In other words, while the primary justification for this project rests on its expected environmental benefits, we believe that net economic returns are not negligible. Furthermore, although the analytical tools for quantifying the consequences of deforestation have still to be perfected, under even the most conservative assumptions the economic costs to the country are enormous--not only the obvious direct costs from loss of forest products (a minimum of US$100 million of wood value is burned every year in Rondonia), but also the longer-term costs associated with soil erosion, flooding, reservoir siltation and climatic changes. Minimizing these costs clearly maximizes the environmental benefits of this project.

9. In summary, the Bank is at a crossroads as far as the Northwest Program is concerned. Either we discontinue our involvement, with obvious repercussions in terms of reactions by the Brazilian Government, the international donor community and major NGOs, or we go forward and take advantage of the opportunity we now have to redirect and strengthen the Program in terms of resource management and protection, bearing in mind that this approach is also not risk-free for the Bank. However, in order to go forward, we <u>must</u> be prepared to finance cocoa and coffee, because the only technical strategy that makes sense for the project area involves planting ecologically acceptable tree crops. Although some diversification is possible, disease, economic and marketing problems in the area currently preclude most alternatives to coffee and cocoa. Furthermore, within this project we must take the existing incentive and marketing systems as given. This reliance on cocoa and coffee may however be only transitional if some of these problems can be overcome. The Bank will soon be actively supporting technology development under a third agricultural research project for the Northeast and North Regions of Brazil, with particular focus on the Amazon Basin. However, these efforts are unlikely to yield widely applicable results during the lifetime of the proposed project. Meanwhile, if tree crops are not established in the agricultural zone 1, the farmers will continue to deforest ever increasing areas in order to plant annual crops and under this scenario large parts of the Amazon will be degraded within few decades. It is clear that the Brazilian Government

cannot hope to reverse this pattern unless it is able to assist farmers to engage in permanent tree crop production on farms of adequate size which will generate reasonable annual incomes.

10. For the reasons described above, the Department requests an exception to the Bank's policy on the financing of cocoa and coffee projects. While there is no denying that aggregate Brazilian production will increase somewhat, the impact of the project on the world market would not be very significant for either crop. The Bank is under constant, heavy pressure to work towards environmentally sound development solutions in the Amazon Basin, and we believe that the proposed project could make a major contribution in this regard. It cannot proceed, however, without supporting cocoa and coffee production.

11. I would appreciate your guidance on whether an exception, on environmental and ecological grounds, can be made to the Bank's policy on financing cocoa and coffee production as soon as possible, so that we may inform the Government as to whether we intend to proceed with project appraisal. If your decision concerning Bank financing of coffee and cocoa is positive, and provided the appraisal mission confirms the Brazilian Government's commitment to meaningful environmental policy reform (para. 6) and the project is economically viable using a more detailed and in depth marginal revenue analysis (para. 8), we would then proceed with loan processing, with a view to presenting this project to the Board in FY90.

cc: Messrs./Mmes.: Dubey (EAS); Lee, Schwermer (COD); Duncan, Akiyama (IECCM); Segura, Selowsky, Garcia-Zamor, Quijano (LACVP); Wessels (LATDR); Piddington, Warford (ENVDR); Goodland (LATEN); Nankani, Koch-Weser (LA1CO); Weissman (LA1DR); Pomerantz, (LA1AG)

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THE WORLD BANK / INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

Date: February 7, 1989

To: Mr. A. Choksi, Director, LA1

From: T. Akiyama, Acting Chief, IECCM TA

Subject: BRAZIL: Rondonia Natural Resource Management Project

1. We have discussed this proposed project with the project staff following Mr. Ducksoo Lee's memo of December 30, 1988. From both an agronomic and microeconomic viewpoint, the project appears to have been thoughtfully designed. As is understood, the project is not consistent with existing guidelines on Bank lending for coffee and cocoa which exclude projects which increase production, except, in the case of cocoa, where the country has no alternative investment opportunities. The expected increase in cocoa, 28,600 tons, is significant in world market terms.

2. The importance of the environmental problem in the project area is acknowledged. However, the Bank has turned down coffee and cocoa projects in many other developing countries under the existing guidelines and other developing countries are watching the Bank's actions on this project to see what kind of precedent will be set. Of particular interest is the fact that we are presently trying to discourage cocoa expansion in the largest producer Cote d'Ivoire, which is much more reliant on cocoa exports than Brazil, the second largest producer. It is unfortunate that the proposed solution to the environmental problem in this case is the expansion of cocoa and coffee production--products with very inelastic world demand. Senior management will have to make a decision on whether this exception will be appropriate. Other points which should be taken into account in their deliberations are the following:

i) The coffee component of the proposed project will include production expansion, out of which 60% will be robustas and the rest arabicas. The expansion of robusta coffee in the project goes against the present trend in the market which is towards the milder, arabica coffees. The price differential between arabicas and robustas widened considerably over the past year or so (robusta prices fell while arabica prices rose) and we are expecting this widened differential to persist for several years, at least. Project staff point out that the increases in production of cocoa and coffee are expected to be consumed domestically because of their lower quality. But this does not nullify the point that they will add to world production of the lower quality cocoas and coffees.

ii) The marginal revenue implications of the project are important because of the size of Brazil's existing output. We estimate that for cocoa the discount that should be applied to our forecast price of cocoa, to take account of the impact of the project on other cocoa production in Brazil, is to be 40% in the short run and 15-20% in the long run. In the case of coffee, given the continued existence of the International Coffee Agreement´s export quota, which supports world prices, calculation of a marginal revenue would not be valid, although, over time, the increased production of coffee will make it more difficult than otherwise to support world coffee prices at a given level. Alternatively, we could assume that there are implicit costs for Brazil in terms of increased storage. To inform management of the marginal revenue implications of the cocoa component, project staff should include calculations of the economic viability using our suggested discount rates of the forecast price.

c.c. Messrs. Qureshi (OPNSV); Dubey (EAS); Lee, Schwermer (COD); Munasinghe (LA1IE); Coirolo, Ms. Pomerantz (LA1AG)

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THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

Mr. Qureshi
RBS 1/4/89

DATE: December 30, 1988

TO: Mr. Rainer B. Steckhan, Acting Vice President, LAC

FROM: Ducksoo Lee, CODDR
D Lee

EXTENSION: 73348

SUBJECT: BRAZIL - Rondonia Natural Resource Management Project
Final Executive Project Summary
December 1, 1988

1. Mr. Qureshi advises that in view of our experience in the POLONOROESTE project, we should make sure that loan preparation and appraisal take account, very carefully, of some of those issues and project dimensions that have caused us problems in the POLONOROESTE project.

2. Specifically, he has the following comments:

(a) the FEPS does not offer a convincing explanation as to how the project will ensure a positive environmental impact. Reference is made to the environmental reforms assured by the Brazilian Government. We must make sure that the proposed agro-ecological zoning and zoning enforcement will be effective in preventing further unauthorized deforestation;

(b) acceptable justification is not provided for the proposed exception to the Bank's policy on the financing of cocoa and coffee projects (a copy of existing guidelines are attached). Also, projects involving these two commodities require endorsement by the International Economics Department, Commodity Markets Division (IECCM) before they are appraised. Such endorsement should be obtained;

(c) in the FEPS there is virtually no information on the nature of the proposed two-year time-slice of infrastructural investments "essential to steer immigrants towards those parts of the State which can support sustainable production." It would be necessary to provide specifics and adequate justification;

(d) in view of the disappointing experience with many resettlement schemes supported by the Bank, there is a need for thorough appraisal of the resettlement component; and

(e) Mr. Qureshi would wish to be provided with a thorough Back-to-Office Report of the appraisal mission within two weeks of its return. He may wish to review this project in the Operations Committee.

cc: Messrs. Qureshi, Vergin, Robless (OPNSV); Sandstrom (AFRVP); Burki (ASIVP); Thalwitz (EMNVP); Husain (o/r)(LACVP); Rajagopalan (PREVP); Fischer (DECVP); Goldberg (LEGOP); Dubey (EAS); Harris (o/r), Casley (o/r), Srinivasan (o/r)(COD)

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WORLD BANK / INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: Files DATE: June 21, 1982

FROM: Alexander Shakow, CPD

SUBJECT: Minutes of Operations Policy Subcommittee Meeting of June 9, 1982

Present:

Members: Messrs. Stern (Chairman), Chaufournier, Goldberg, Kirmani, Knox van der Meer, van der Tak, Vergin, Wapenhans, Wiehen, Wright

Others: Mrs. Hughes, Messrs. Yudelman, Waide, Chernick, Duncan, Scandizzo, Horsley, Kopp, Ms. Pratt, Mr. Shakow

Bank Group Financing of Tea, Coffee and Cocoa

1. The OPSC reviewed a memo which proposed an interim procedure for lending decisions on tea, coffee and cocoa while awaiting the design and testing of a new approach which would include global cost-benefit analysis at an early stage of project identification. (This proposal emerged from discussions between EPD, AGR and others in the Bank in response to the July 15, 1981 OVP decision to restrict lending for these commodities.)

2. The OPSC agreed that the proposed Interim Guidelines should be modified so that they can serve as a statement of current policy. First, to simplify the cocoa conditions, the guidelines will read:

> "8. The Bank will finance projects involving production of cocoa only if they will not lead to increases in exports. Exceptions will be made for projects meeting normal Bank criteria only - i) in countries where the output level is much below historical levels due to major disruptions in production patterns, or ii) in low-income (i.e. IDA-eligible) countries without economically viable alternatives."

(This eliminates a provision in the draft which required that exceptions meet normal Bank economic rate of return criteria "even after discounting the projected world price by 50 percent", a condition OPSC members thought was unnecessarily arbitrary.)

3. Second, the members clarified the proposed panel review system and agreed that appraisal missions for projects involving these crops should not leave until there is agreement between the relevant project department, EPD and AGR that the project meets the interim lending guidelines. This agreement, achieved as early in the project cycle as possible, should be reflected in the final project brief before appraisal. The attached Interim Guidelines reflect these OPSC decisions.

4. AGR, in consultation with EPD, is preparing a new methodology to extend existing economic rate of return analysis to allow for the impact of Bank-financed projects on the real income of producers and consumers in other developing countries. While the OPSC agreed that the proposed study of a new methodology should proceed, members expressed skepticism as to the ultimate feasibility and usefulness of this approach. Members were especially concerned about the implications for other commodities - e.g. iron ore - also facing inelastic demand: where would the line be drawn once an explicit methodology was used to measure impact on other countries of Bank projects? Members were thus unsure that such an approach, even if the data and technical aspects proved manageable, would help significantly in making project decisions. In addition, it was noted that indirect Bank assistance to these crops in the form of road or water projects would not be judged using this methodology.

On the other hand, AGR and others noted the possibility that the methodology, once prepared and tested, could be helpful to project decisions - and only when a proposal had been prepared could a judgment be made. It was also pointed out that such a methodology could help Bank policy advice on prices, tariffs, etc. and increase the consistency between Bank lending and policy advice.

5. In summary, it was agreed a) that the attached guidelines (Annex A) would serve as a restatement of existing Bank policy on the three commodities, and b) that AGR, in consultation with EPD, ERS and the regions would prepare and test the methodology for global cost-benefit analysis for tea, coffee and cocoa; when it was ready (estimated to be within the next 6 months) it would be sent through the normal review process for consideration by the OPSC. At that time, any proposed changes in policy and procedure would be considered.

Attachment

Cleared by: Mr. Stern

AShakow/ww

ANNEX A: LENDING GUIDELINES FOR BANK GROUP FINANCING OF TEA, COFFEE AND COCOA PROJECTS

1. This note sets out the procedure to be followed for all projects, including comprehensive rural development projects, which include significant production of tea, coffee or cocoa. Before appraisal teams leave Washington, AGR EPDCE and the relevant Projects department will agree (and reflect in the project brief) that the project adheres to these lending guidelines.

Tea

2. Consistent with existing Bank guidelines[1/], the Bank Group will not finance projects involving production and processing of tea, except for:

i) increases in output in countries with no investment alternatives yielding an acceptable rate of return; and

ii) rehabilitation involving no increase in output (this implies a reduction in acreage and encouragement to diversification).

Projects for diversification out of tea production will be encouraged where economically feasible, particularly in countries with large shares of the market. If an affective International Tea Agreement is negotiated, financing of increased production can take place within the framework of the Agreement.

Coffee

3. The Bank Group should normally not lend for coffee projects, except:

i) for crop diversification out of coffee and for rehabilitation of plantings affected by sudden and recent damage by disease or weather, for quality improvements or for new plantings which replace output from other areas; and

ii) such projects should be undertaken only if they do not lead to increases in total production in the borrowing country in excess of projected increases in (a) domestic consumption plus (b) International Coffee Organization (ICO) quota exports plus (c) exports to non-ICO countries.

4. Almost all coffee-producing countries are members of the International Coffee Agreement and are therefore subject to export quotas. For small coffee-producing countries (i.e. producing less than 400,000 bags of 60 kg. annually), the rate of expansion of their export quota is specified in the Agreement. For other countries, export quotas are set annually by the International Coffee Organization, but their long-term expansion is determined by the growth in world import demand.

1/ Bank Group Financing of Tea, Board Paper, August 17, 1973; reaffirmed in Bank Financing of Tea: A Reappraisal, February, 1979.

5. Application of the above guidelines would mean that domestic consumption and export growth must be forecast for each potential borrowing country, with exports including those to non-ICO countries as well as to ICO-importing members. It also means forecasting the future growth of production in each potential borrowing country, to determine if future production is likely to be in harmony with expected total demand. Such forecasts are already provided by EPDCE.

6. According to the most recent Bank analysis of the coffee market (reported in the Technical Annex to the draft Policy Paper) 1/, world production of coffee cannot grow on average faster than about 1.3% per annum for the next 10 years if the intervention "floor" price is to be maintained at its present level in real terms. For the time being, this should be the norm against which the expected production of each potential borrower is assessed, with appropriate allowances made for ICO export quota allocations, for export growth to non-ICO countries and for potential growth in domestic consumption.

Cocoa

7. There are no export quotas within the International Cocoa Agreement (ICA). The ICA seeks to stabilize prices by buffer stock purchases and sales. Unlike the Coffee Agreement, the ICA does not cover all significant producing and exporting countries.

8. The Bank will finance projects involving production of cocoa only if they will not lead to increases in exports. Exceptions will be made for projects meeting normal Bank criteria only i) in countries where the output level is much below historical levels due to major disruptions in production patterns or ii) in low-income (i.e. IDA-eligible) countries without economically viable alternatives.

June 21, 1982

1/ T. Akiyama and R. Duncan, Analysis of the World Coffee Market, EPDCE, November, 1981, annexed to World Bank Group Financing of Tea, Coffee, and Cocoa, EPDCE, February, 1982

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: December 8, 1988

TO: Mr. S. Shahid Husain, Vice President, LAC

THROUGH: Mr. Armeane M. Choksi, Director, LA1 AMC

FROM: Phyllis Pomerantz, Acting Chief, LA1AG PRP

EXTENSION: 31907

SUBJECT: **BRAZIL - Proposed Rondonia Natural Resource Management Project 1/ Final Executive Project Summary**

1. Attached please find the Final Executive Project Summary and the Minutes of the November 2, 1988 Regional Loan Committee meeting on this project. In your review of the attachments, I would like to draw your attention to three key points summarized below.

2. Type of Lending Instrument. As you may recall, in the context of this project, the Brazilian Government has undertaken (April 29, 1988 letter from the Minister of Interior to Mr. Conable) to implement a package of environmental reforms designed to modify the policy/regulatory framework in Rondonia so as to ensure that future Government interventions and private initiatives are channelled only into sustainable and environmentally sound economic activities. The Department initially recommended a hybrid loan approach, with approval of all major legislation/regulations in the policy package as a requirement for a single tranche disbursement of about US$65.0 million. The balance of US$85.0 million was to finance the State's five-year agricultural development program. Nonetheless, because of the uncertain macroeconomic situation, and at the recommendation of the Regional Loan Committee, we have opted instead for a standard investment project. In order to transfer an equivalent amount of resources (commensurate with the importance of the policy reform package to be implemented in Rondonia), we have widened the scope of the project to include time-slice financing of the State's medium-term investment program. About 60% of the proposed loan (of US$150 million) would finance a five-year program of agricultural and environmental activities, with the balance supporting a two-year time-slice of infrastructural investments essential to steer migrants towards those parts of the State which can support sustainable production. The Bank would conduct a detailed appraisal of all the agricultural and environmental activities to be financed under the project and of the consistency of the state's entire investment program with the agro-ecological zoning to be agreed to under the project. Brazilian authorities would appraise other investments in the program based on criteria agreed with the Bank.

1/ **Originally called Northwest Consolidation Project - State of Rondonia; and now re-named Rondonia Natural Resource Management Project.**

3. Timing of Operation. To allow time for counterpart funding decisions (relating to "Operacao Desmonte", Congressional deliberations on the 1989 budget, Ministry of Finance policies concerning allocation of discretionary Federal resources, and the Government's review of its own policies in the area of environment), the appraisal of this project has been delayed, at the request of the Government, from November 1988 to January 1989. If the Federal and State Governments confirm availability of adequate counterpart funds by mid-January, and if the Government's own review is completed by then, all possible efforts will be made to deliver this project in late FY89. However, there is considerable risk of further delays because of the counterpart funding issue and the extremely tight timetable for loan processing.

4. Financing of Coffee and Cocoa. Preparation of this project has involved a major agro-ecological zoning effort to subdivide the State into different zones based on identifiable classes of land use potential, and then to derive appropriate development strategies for each identified zone. The resulting recommendations for those areas with the best potential for sustainable agriculture are based on intercropping of perennial crops (principally cocoa, coffee and rubber), and agro-forestry. From an environmental standpoint, any deviation from this strategy in Rondonia (or in many other parts of the Amazon Basin) would be extremely detrimental to the region's natural resource base, with obvious and well understood consequences both for Brazil and the international community (e.g., climatic changes, loss of biodiversity). The appraisal mission would carefully analyze the Government's production estimates, but it is likely that the results will indicate some incremental exports of both cocoa and coffee. In that event, a decision will be needed as to whether, in the interests of supporting sound environmental objectives in the Amazon Basin, the Bank would be willing to relax existing restrictions on financing of these surplus commodities.

5. Your approval for the appraisal of this project in late January 1989 is requested.

Attachments

cc: Messrs./Mmes.: Qureshi (2) (SVPOP); Shihata (VPLEG); Selowsky, Linder, Quijano, Segura, Garcia-Zamor (LACVP); Inakage (VPCOF); D. Lee (CODDR); Rajagopalan (VPPRE); Petit (AGR); Wessels (2) (LATDR); Weissman (LA1DR); Goodland (LATEN), McGarry (LATEN); Nankani, Seade, Schneider, Koch-Weser (LA1CO); Papageorgiou (LA1TF); Munasinghe (LA1IE); Birdsall (LA1HR); Collell, Manley (LEGLA); Barahona (LOAEL); Rovani (DGO); Papadopoulos (LA1BR)

LCoirolo/mg

December 1, 1988

FINAL EXECUTIVE PROJECT SUMMARY

BRAZIL: RONDONIA NATURAL RESOURCE MANAGEMENT PROJECT

Borrower:	Federal Government of Brazil			
Beneficiary:	State of Rondonia			
Financing Plan:	Government	-	US$150.0 million	(50%)
	Bank	-	US$150.0 million	(50%)
			US$300.0 million	(100%)

Tentative Appraisal Date: January 1989 **Tentative Board Date**: June 1989

1. **Background**. In 1981, with the participation of the World Bank, the Brazilian Government launched the POLONOROESTE Program in the Amazonian agricultural frontier areas of Rondonia and Western Mato Grosso. In its first years, POLONOROESTE failed in many respects: only pavement of the BR-364 highway, the Program's centerpiece, proceeded on schedule, while agricultural and social support services and environmental protection fell behind. Limited knowledge of the natural resource base, a steep increase in migration to the region, weak institutional capability of executing agencies, and the prevailing policy and regulatory framework all caused a rapid expansion of precisely those forms of destructive land development which the Program was supposed to discourage. The deforested area in Rondonia increased from 3% of the State in 1980 to 24% in 1988.

2. As the environmental consequences of accelerated occupation became obvious, some significant steps were taken to correct POLONOROESTE's initial shortcomings. Key institutions have been created/strengthened, and there has been a growing political commitment to preserve the region's remaining natural resources. Equally important, recent advances in technical knowledge now make it possible for Rondonia to use agro-ecological zoning in its development planning. Agro-ecological zoning identifies different areas according to potential land use, distinguishing those which are capable of sustainable development from those without any known long-term potential or which have special ecological or social (Amerindian lands) significance and therefore need to be protected. State and Federal authorities have now agreed to introduce major policy reforms and modify their investment programs for Rondonia, based on agro-ecological zoning. These reforms have been detailed in a letter dated April 29, 1988 from the Minister of Interior to Mr. Conable. Some important measures have already been adopted in the interim.

3. **Rationale for Bank Involvement**. The Bank's lending program for Brazil places increased emphasis on a wide spectrum of environmental issues (soil erosion, depletion of renewable resources, air and water pollution from industrial waste, etc.). With regard to the Amazon, despite the serious problems encountered by the earlier POLONOROESTE projects, based on new agronomic knowledge and lessons learned to date, the Bank is in a better position today than in the past to support Brazil in fostering a more rational development of that region. A distinguishing feature of project design, facilitated by Bank participation and largely missing from earlier POLONOROESTE operations, would be the explicit effort to adapt the policy and institutional framework and investment plans for Rondonia, so as to make them more supportive of sound natural resource management.

4. **Project Objectives**. The principal objective of the proposed project would be to test a new approach--shaped by difficult past experience--to managing development in one State (Rondonia) of the environmentally fragile and politically sensitive Amazon Basin. The project would assist the Government to: (a) institute changes in policies/regulations and public investment programs which have been responsible in the past for much of the uneconomic investment and unnecessary resource destruction in Rondonia; (b) support key investments needed to implement agro-ecological zoning in Rondonia; (c) consolidate the technical and operational capacity of key institutions, particularly those responsible for agricultural and forestry support services and protection of ecological and Amerindian reserves; and (d) provide a model for development of other environmentally fragile areas in Brazil.

5. **Project Description**. The proposed loan (US$150 million) would finance a time-slice of the overall Federal and State investment program for Rondonia. About US$90 million would support the State's five-year agricultural development and environmental protection program including: (a) land regularization, zoning and mapping; (b) agricultural research; (c) agricultural extension; (d) agricultural credit; (e) agricultural marketing; (f) road maintenance; (g) forest management; (h) management and protection of conservation units, Amerindian reserves and environmental protection; and (i) monitoring, project administration and training. The balance of the loan would be used, during the first two years, to finance infrastructural investments essential to steer migrants towards those parts of the State which can support sustainable production, as identified in the agro-ecological zoning. The Bank would conduct a detailed appraisal of all agricultural and environmental activities to be financed under the project; Brazilian authorities would appraise other investments under the project based on criteria agreed with the Bank (e.g., consistency with agro-ecological zoning, existing Bank sectoral policies and procurement arrangements for Brazil, economic viability and fiscal sustainability). The project would focus on consolidation of already occupied areas and would pay particular attention to strengthening key executing agencies.

6. **Issues and Actions**. Agreement should be reached at appraisal and confirmed at negotiations on the following items: (a) that a satisfactory policy and institutional reform package should be in place by negotiations; (b) that the five-year Federal and State investment programs for Rondonia would be consistent with agro-ecological zoning and that the Bank would review annual implementation plans and budget proposals; and (c) that the credit component, which the State proposes to denominate in kind, should be consistent with current Bank/Government agreements concerning relending mechanisms, terms and the financial capability of participating banks. Finally, appraisal estimates may show some incremental exports of both cocoa and coffee; in that event an internal decision would be needed as to whether, in the interests of supporting sound environmental objectives in the Amazon Basin, the Bank would be willing to relax existing restrictions on financing these crops.

7. **Benefits**. The project would support activities to enhance the financial and economic viability of environmental protection. Specifically, it would promote sustainable agricultural production of high value crops in areas of good soils, where slash and burn shifting cultivation of mainly annual crops has been the practice. Extractive activities, with renovation/enrichment, would be supported in areas with low agricultural aptitude, which would otherwise be deforested and left with depleted soil fertility in 5-6 years' time. Under even the most conservative assumptions, a minimum of US$100 million of wood value is burned every year in Rondonia, without quantifying the longer-term costs associated with soil erosion, flooding reservoir siltation and climatic changes induced by deforestation.

8. **Risks**. Given current technical knowledge, particularly the availability of agro-ecological zoning as a tool for development planning in Rondonia, and existing political commitment, the prospects for Bank involvement in POLONOROESTE are much better today than in the past. With regard to the proposed policy and regulatory reforms to be instituted under the project, every effort has been made to identify the most important causes of past environmental degradation in Rondonia. Nonetheless, there is a high risk that unforeseen and unforseeable factors could undermine the impact of these reforms. To the extent possible, appropriate monitoring and evaluation devices, to be financed under the loan, would therefore be in place at the start of project execution. There is also a risk to the Bank of continued adverse publicity if the project fails; on the other hand, to phase out of the Northwest at this time would still leave the Bank vulnerable to criticism for whatever future environmental damage occurs in Rondonia, since it was so actively engaged in the start-up of POLONOROESTE. Moreover, if the project is designed as indicated above, with policy reforms preceding other activities, we expect the risks to be minimized.

July 14, 1989

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THE WORLD BANK
Operations Committee

MAURITANIA

COUNTRY STRATEGY PAPER

POSTSCRIPT

138. The Operations Committee met on July 14, 1989, to consider the Mauritania CSP. The discussion, while following the agenda, concentrated on: (a) Mauritania's economic and financial viability in light of its modest growth potential, extremely high indebtedness and recent social disturbances; (b) the realism of projected external assistance; and (c) the structure of the proposed lending strategy.

139. The Committee took note of the country's little developed potential in irrigation, good prospects in fisheries and the possibility of increased private sector activities financed in part by emigrants' remittances, offering prospects of gradually declining dependence on official foreign aid. It was also stressed that, in spite of recent disturbances, the private sector continued to invest in irrigation and fisheries, thus presenting an encouraging alternative to largely failed public ventures.

140. With regard to the future volume of external assistance, it was concluded that this largely depended on the outcome of the donors' meeting at the end of July. The outcome would depend very much on the Government's position regarding the social disturbances that had caused serious difficulties between Mauritania and Senegal. This would be reported back to the Committee for further consideration and a final decision on the Bank's lending strategy.

141. Concern was expressed regarding the skewing of the proposed lending program towards adjustment lending, particularly in the context of the proposed restructuring and financial workout of SNIM, the iron ore company, to secure the servicing of an IBRD debt. It was agreed that the justification for the SNIM operation as set out in the CSP should be strengthened and reviewed on the economic and financial merits of the project. The question of a core lending program was also discussed.

142. The final decision on the lending program was postponed till after the donors' meeting. The outcome of that meeting will be taken into account in the final design of the lending strategy. The decision will be reflected in an additional postscript to the CSP.

UThumm:sb

July 20, 1989

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THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: July 11, 1989

TO: Operations Committee

FROM: Anandarup Ray, Acting Director, EAS

EXTENSION: 78073

SUBJECT: MAURITANIA - Country Strategy Paper; Agenda

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1. The Operations Committee will meet on **Friday, July 14, 1989, at 2:30 p. m. in Room E1243** to consider the Mauritania Country Strategy Paper. The following represents a proposed agenda for the meeting.

Background

2. Mauritania is a large but sparsely populated country with a limited resource base. With a per capita GDP of US $440, it is at the top of the category for the lowest income countries of Africa. The economy is highly dependent on agriculture and extensive livestock farming. The exports are principally iron ore and fishery products.

3. In recent years, it has experienced declining real per capita output. Beset by inadequate economic management and limited administrative capacity and undertaking relatively ambitious programs financed by external debt, the country nurtured a large and inefficient public sector. Mauritania undertook economic adjustment in 1985 with the help of IDA and the Fund. Under its Economic and Financial Recovery Program (PREF), the Government adopted a flexible exchange rate policy, a program for improving public sector management, an investment and rehabilitation program, and an incentive framework to promote private sector activities.

Macro-economic Adjustment and Commitment to Reform

4. Mauritania is currently undertaking a medium-term program under a PFP framework. The Committee may want to ask the Region to provide an update on the macro-economic situation, and to elaborate upon the Government's performance and commitment to reform given that the country has experienced "stop-and-go" reform measures and frequent changes in key officials (para. 30).

5. The country recently experienced civil disturbances connected with ethnic issues. The Committee may want to ask the Region about the implications of these problems for medium and long-term strategies and for the Bank's program of country assistance.

6. Mauritania's development potential is limited by its geography and inadequate resource base. The Committee may ask the Region for its assessment of the potential sources of growth. What is the comparative advantage of the country and what sources of domestic growth are envisioned in the development program?

Bank Assistance Strategy

7. The CSP proposes a lending program that is composed mainly of policy-based operations with quick-disbursing assistance. Thus, the strategy is premised on a combination of SALs, SECALs and hybrid operations. The Region argues in favor of this approach in view of the limited amount of Bank assistance (about 10% of total expected flows) and a limited Regional staff capacity to work on specific investment operations. The Committee may ask the Region to elaborate upon the proposed strategy, especially in connection with the following issues:

- what has been the experience with adjustment operations thus far? What is the basis for our optimism regarding the country's ability to carry out policy reforms?

- would the sector reforms to be supported by the series of sector adjustment operations have sufficient budgetary and balance of payments justification to warrant quick-disbursing assistance?

- Is there an appropriate balance between quick-disbursing lending and investment lending? Given the country's weak administrative and planning capacity, should not the Bank's resources and leverage be more useful in supporting investment planning and coordination? What assistance is being planned to strengthen the Government's absorptive capacity?

Resource Mobilization and Financial Requirements

8. A "moderate adjustment scenario" -- the preferred or base case scenario -- is used as the basis for the projections of financing requirements in the CSP. The operations envisaged under this scenario are listed in Annex D (the program to be pursued under the non-adjustment lending scenario is also shown in this table).

9. The base case scenario assumes that macro-economic and sector reforms will be in accordance with the PFP. This program assumes that investments will be 16% or 17% of GDP, of which public investment will be 12% of GDP. The projections of external financing requirements are contained in para. 94. The financing plan assumes a major rescheduling of debt in 1989 and 1990 in the range of US $274 to $372 million. In 1988, Mauritania's debt service ratio was 59% of exports; this is expected to fall to about 33%, with debt rescheduling and some debt forgiveness, by 1993.

10. The Committee may want to ask the Region how realistic are the assumptions underlying the base scenario, especially those on aid projections, export earnings, and the ICOR. Are the investment targets for the country too high in view of the country's limited fiscal resources? To what extent are domestic resource mobilization issues being addressed in the adjustment program and how do they bear on the low and high adjustment scenarios?

11. The Committee may also want to be briefed about burden-sharing, especially in view of the reduction in Arab economic assistance. The Region might also explain what it proposes to do to avoid default on the IBRD loan to the iron ore enterprise.

Programs of Special Emphasis

12. The Region may want to explain precisely how the concerns with environment, population and women-in-development are integrated into proposed lending operations and economic and sector work.

cc: Messrs./Mmes Qureshi, Shihata, Rajagopalan, Fischer, Wood, Jaycox, Karaosmanoglu, Thalwitz, Husain, Vergin, Gillette, Lee, Shakow, Holsen, Rao, Burmester/Thahane, Hinkle, Steer, Baudon, Jonas.

For Information Only

cc: Messrs./Mmes Hopper, Frank, Parmar, Goldberg, Bock, Pfeffermann, Baneth, Kavalsky, Aguirre-Sacasa, Haug, Tanaka, Robless/Lawrence, Agarwala.

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GSicat/:sb:vlw

July 17, 1989

THE WORLD BANK
OPERATIONS COMMITTEE

CONFIDENTIAL

BOLIVIA

COUNTRY STRATEGY PAPER

Postscript

106. The Operations Committee met on July 17, 1989 to discuss the CSP for Bolivia which proposed a lending program of $410 million over the 1990-94 period. The discussion broadly followed the agenda prepared by the Economic Advisory Staff.

107. The discussion focussed on the uncertainties affecting adjustment program. These include the forthcoming political change, the volatility of tin and gas prices, and the difficulties of receiving payment from gas sales to Argentina. The success of the recent stabilization effort was noted as well as the fact that supply responses have yet to occur on a significant scale. The Chairman suggested that the priorities of the Bank's program should be presented on a more selective basis, and that the trigger points for revising the lending program should be indicated in more specific terms. He also stated that if the availability of IDA funds at the level indicated in the CSP cannot be assured, the overall lending strategy would need to be reviewed.

108. The issue of growth versus poverty while generating a reasonable growth scenario was addressed. For this the policy reform process needs to be deepened with a switch to the productive sectors to help remove supply side constraints. The poverty impact was being strengthened not by proposing increases in expenditure on the social sectors but rather by reallocations of current levels of expenditure towards the poor. It was noted that there are major environmental as well as financial costs to establishing a new growth pole through agricultural development in the lowlands. The Chairman agreed that environmental concerns should be emphasized in the program for bringing new lowland areas into cultivation.

109. The interaction between the coca cultivation, the drug economy and the economic prospects were discussed. It was noted that increased coca leaf production in neighboring countries coupled with reduced demand is likely to lead to a significant decline in Bolivia's foreign exchange earnings from coca now estimated at US$500-600 million per year. Alternative sources of growth are essential. The need for looking into the costs and benefits of moving away from coca, not just in Bolivia but in the LAC region more generally, was discussed. However, the magnitude of the problem and the Bank's ability to carry out such a study was questioned.

110. With respect to debt and finance, the advantages of debt buy-backs were noted, and questions were raised about what would happen if the assumed IDA allocations were not forthcoming. It was noted that IDB funds cannot substitute easily because soft terms are currently only available for social projects. It was suggested that any proposal for debt reduction should look not just at commercial debt but at the overall debt structure and debt management strategy, including the possibilities of obtaining Toronto terms for Bolivia.

111. As regards the proposal to raise the current ceiling on project cost-sharing, the Chairman stated that the present ceiling should be maintained. The subject, he felt, needs to be reviewed by the Central Operations Department on a cross-country basis.

ARay:vlw
July 17, 1989

LIST OF PERSONS ATTENDING THE OPERATIONS COMMITTEE MEETING

BOLIVIA - COUNTRY STRATEGY PAPER

MONDAY, JULY 17, 1989 AT 10:30 A.M. IN ROOM E-1243

Committee Members

Messrs. A. Karaosmanoglu - Chairman
A. Stoutjesdijk - EMNVP
S. O'Brien - AFRVP
J. Linn - DECVP
D. Goldberg - LEGVP
J. Wood - FPRVP
H. Vergin - OPNSV

Other Attendees

Messrs. V. Dubey (EAS)
A. Ray (EAS)
E. Barandiaran (LACVP)
P. Loh (LA3DR)
K. Marshall (LA3C1)
W. Shaw (LA3C1)
S. Jorgensen (LA3C1)
R. Drysdale (LA3HR)
T. Thahane (SEC)
O. Yenal (ASIVP)
M. Molares (LEGLA)
A. Heron (CODOP)
F. Lysy (LA3C1)
E. Wetzler (CL2C1)

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THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: July 10, 1989

TO: Operations Committee

FROM: Anandarup Ray, Acting Director, EAS

EXTENSION: 78073

SUBJECT: BOLIVIA - Country Strategy Paper - Agenda

1. The Operations Committee will meet on Monday, July 17, 1989, at 10:30 a.m., in Room E-1243, to discuss the Country Strategy Paper for Bolivia.

2. At the time the administration of President Paz Estenssoro came to power in 1985, Bolivia was in a deep crisis. GDP had dropped by about 25% since 1980 and the inflation rate exceeded 20,000 percent per year. The economy was highly controlled, there were severe trade and payments restrictions, and large external arrears. The economic recovery program that Estenssoro initiated in late 1985 succeeded in stabilizing the economy, and there was some GDP growth in 1987 and 1988 after many years of decline. However, the decline in per capita consumption levels has not yet been arrested.

3. There has been some policy slippage during the last year. Inflation was 21.5% in 1988 rather than the programmed 12.5%, and the real exchange rate appreciated, albeit by a small amount. There were large net capital outflows in 1988. The fiscal deficit widened during the first quarter of this year. Planned reductions in average tariff levels have been postponed, there have been delays in adjusting public sector prices, the program to privatize some of the public enterprises has made little progress, and the planned improvements in incentives for private sector investments have not been completed. With the new administration scheduled to take office in August, the CSP correctly identifies the "viability and durability of the present Government's achievements" as the major concern at this point.

Issues

4. This CSP presents four "scenarios" to illustrate the possible effects of different degrees of policy effort (Table 1). In addition to the conventional "base" and "low" cases, two upside and downside extremes have been added. These do not indicate Bolivia's vulnerability to external shocks, however. There is another scenario in Table 6, which reflects the possible effects of a 25% drop in the prices of tin and natural gas. This is the only external contingency considered. There are several sets of issues that the Committee might consider with reference to these quantitative illustrations:

- the realism of the base case. The Region's base case is more conservative than the one adopted by the IMF due to more conservative assumptions on Argentina's willingness to pay for natural gas and on capital inflows. Nonetheless the Region might comment on how confident we can be regarding the acceleration of the growth rate in the near term. In particular, the Region might comment on (a) the prospects for 3.5% growth in 1989 and 4% growth in 1990, given the emerging needs for controlling aggregate demand; (b) the realism of a 10% growth rate in non-traditional exports during 1989-97 (past data are not provided for that group); and (c) the jumps in domestic savings and investments (over 40%) assumed in the base case during 1988-90. One notes that the declining trend in private investments during the 1980s has barely been reversed. Annex 4 indicates high optimism regarding marginal savings rates; it also suggests possible optimism regarding the ICOR;

- "acceptability" of the base case and policy leverage. While the Region characterizes the base case as "acceptable", one must note that it implies continuously declining per capita consumption levels until 1997. This implication of the base case also raises questions regarding its viability. However, the Region also believes in the high potency of better policies, as a comparison of the base case with the "high" case shows. The Region has identified two crucial policy variables in this context: better incentives for private sector investments and rapid improvements in public sector administration. Can the Region specify concrete measures that the new administration should take to move towards the "high" case, in contrast to the base-case measures we have included in the draft PFP? What can be done, for example, to rapidly improve Bolivia's ability to use external resources (undisbursed commitments of foreign aid totals $1 billion at this time)? What can the Bank and the other donors do by way of technical assistance? Do the Bank and the IMF agree on the additional policy measures required in the "high" case, and are they to be discussed with the Government in the PFP context?

- downside scenarios. The two downside scenarios reflect policy slippages. In the "low" case, IDA will respond to policy slippages by adopting the "core" program shown in Annex 1B, and in the very low "disaster" case lending will cease. But these two cases do not fully reflect risks because Bolivia is also extremely vulnerable to adverse external shocks: a combination of a 25% price drop with only moderate policy slippages can, for example, lead to very adverse results. Another important source of risk is Argentina's ability or willingness to make timely payments on natural gas and to renew the contract at favorable terms. The Region might elaborate upon (a) the overall risk of Bolivia getting into non-accrual status with IDA; (b) anything the Bank and the Fund can do to moderate the impact of adverse external shocks, such as helping to create a fund for stabilizing export earnings; and (c) the appropriateness of the planned "core" program. While the importance of fighting poverty can hardly be exaggerated, it may be more appropriate to design a highly-productive, foreign- exchange earning core program instead. This is because per capita incomes would be declining rapidly in the core-program scenario, and specializing on social projects would be like running up a down escalator; there would also be a serious default risk in that scenario;

- level of concessional assistance. Bolivia's performance during the last four years has generally been highly rated, but access to concessional finance may not have been fully commensurate; it has not, for example, received Toronto terms or debt cancellations. Even within IDA its "norm" share is less than it would be without the Africa pre-allocation. The Region might explain what the financing gap is and what our assumptions are regarding sources of finance and burden-sharing, especially if adverse contingencies occur. With respect to IDA, the Region's proposal for an annual average of US$82 million beginning in 1990 is considerably higher than the annual average recommended by SPR/OPS. One issue is whether the higher size would be justified; another is whether we should plan for a graduated response. If Bolivia's performance improves, we might want to be able to respond with higher levels of IDA. We might therefore plan on a smaller level in the base case;

- debt strategy and debt buy-back. The CSP mentions "distinct advantages" to extinguishing the remaining commercial bank debt through new buy-back operations (page ii), but the advantages are not spelled out. Since Bolivia has not serviced commercial bank debt since 1984, and, according to the CSP, will not be able to afford new commercial borrowings for a long time, the Region might explain the benefits of another buy-back at this time. This is important because Bolivia would be a candidate for additional IDA resources from the proposed debt-reduction fund;

5. In addition to these issues, the Committee might also wish to focus on the following:

- the CSP puts great emphasis on income-redistribution and poverty-redressal objectives. The sharp disparities in income and social development between the elite and the poor Indian populations, as well as absolute poverty, have become accentuated due to the overall decline of the economy. How are poverty-alleviation and equity objectives specifically pursued within the operations proposed in the lending program? How are these objectives reflected in Bolivia's current and capital expenditure programs? In view of the great need to raise savings, investments and growth, what is the scope for social programs that are complementary to growth?

- the CSP proposes financing of up to 85% of project costs, with a maximum of 90% taking cofinancing into account. This is only a modest increase from the current ceiling of 80% without cofinancing, but the proposal is not explained at all in the paper. There are many countries with similar or lower per capita incomes with lower ceilings on project cost-sharing. For example, the Philippines, Sri Lanka, Ghana and Nigeria have ceilings on cost-sharing of 75%;

- the importance of the drug traffic for the Bolivian economy. It is noted that total recorded receipts from cocaine exports is probably as large as all other exports. It is not clear, however, how the cocaine issue has been reflected in the projections. Furthermore, the Committee might consider whether our posture on the cocaine trade has been appropriate;

- to what extent environmental concerns feature or should feature in our policy dialogue and lending operations?

6. The Committee might recommend a CSP update early next year after we ascertain the plans and capabilities of the new administration.

OC Members

Messrs. Qureshi, Husain, Jaycox, Karaosmanoglu, Thalwitz, Rajagopalan, Fischer, Shihata, Wood, Vergin.

cc: Messrs. Lee, COD; Shakow, Liebenthal, SPR; Holsen, CEC; Rao, Steer, FRS; Burmester/Thahane, SEC; Baudon, OPNSV; Hopper, PPR; Bock, DFS; Goldberg, LEGOP; Kavalsky, FRM; Parmar, CIO; Pfeffermann, CEI; Baneth, IEC; Robless, OPNSV; (Ms.) Haug, Tanaka, EXC; Aguirre-Sacasa, EXT; Selowsky, Loh, (Ms.) Marshall, Miovic, Potashnik, LAC.

ARay:vlw

July 7, 1989

890717020

THE WORLD BANK

OPERATIONS COMMITTEE

CONFIDENTIAL

Minutes of the Operations Committee Meeting to consider AFRICA: Long Term Perspectives Study held on July 7, 1989 at 4.00 p.m. in Room E-1243

A. Present

Committee

Messrs. M.A. Qureshi (Chairman)
S. Husain (LACVP)
K. Jaycox (AFRVP)
A. Karaosmanoglu (ASIVP)
W. Thalwitz (EMNVP)
S. Fischer (DECVP)
I. Shihata (LEGVP)
D.C. Rao (FRS)
H. Vergin (OPNSV)

Others

Messrs. R. Agarwala (AFTSE)
B. Alisbah (AS4DR)
P. Dufour (FRM)
J. Holsen (CEC)
J. Katz (FRM)
P. Landell-Mills (AF1CO)
R. Liebenthal (SPRPA)
C. Obidegwu (APRPA)
S. Rajapatirana (EAS)
A. Rigo (LEGAF)
C. Robless (OPNSV)
U. Thumm (EAS)
H. Wyss (AFTDR)

The Committee met to discuss the green cover of the Africa: Long Term Perspectives Study. The EAS had prepared an agenda for the meeting.

B. Issues

Given the global approach taken in the study to define development issues in Africa, the thirty year perspective and the wide range of topics covered in the study many issues were discussed. These were, the global approach to analyzing Africa's development problems, the macroeconomic projections that underpinned the foreign aid requirements, the amount of aid flows, development strategies proposed, agriculture sector, regional integration, equity versus poverty alleviation and statistical issues.

C. Discussion

The Chairman invited the Region to introduce the study before the Committee, noting the interaction with African leaders in the preparation of the study and asked the Region to describe the present status and the plans for completing the study.

The Regional staff described the genesis of the study noting that there was a demand both from within and outside the Bank to look beyond the medium term for stimulating growth in Africa. This demand arose from the various adjustment operations in place, the special programs under implementation and from external donors who wanted to take into account African perspectives in defining a program for growth. In preparing the study, an interactive process was followed with African leaders, institutions and donors which was by its very nature risky when a consensus was sought among the different parties to diagnose the problems and define solutions. Several workshops were held with different parties which gave a sense of participation to all involved. Due to this sense of participation, many African participants made criticisms of governance in Africa, styles of government and corruption hitherto eschewed by them. Due to the consensus seeking process, the Bank could not unilaterally modify the positions that had been reached regarding the major problems and solutions. The Economic Commission for Africa has put out a report recently that partially reflects the emerging consensus. On the other hand, the ECA report characterizes the Bank and IMF's adjustment programs undertaken in Africa as failures. However, there is nothing the Bank can do about this, except to maintain its high standards of analysis.

The Region proposes to hold an informal seminar on the study with the Bank's Board during the summer and hold a more formal Board seminar by the end of 1989 to finalize the study.

The Chairman invited the Regional staff to present the main themes of the study. The Regional staff indicated that the starting point for the analysis was the need to achieve an output growth rate of 4% per year to raise per capita income, given that population would grow at 3% per year. Agriculture was to be the major source of growth. However land was becoming a constraint and there was a need to increase agricultural productivity through changes in technology. To realize the target GDP growth rate, investment rates had to be increased from their present depressed levels. The decline in efficiency of investment as measured by the inverse of the incremental capital output ratio (ICOR) had also to be arrested and efficiency raised. Two major themes of the study to achieve these targets were to improve the enabling environment and to improve capacity. The latter was to be achieved via increased investment in human resources. The earlier development strategy, had not paid enough attention to improving human resources. The high cost found in Africa was due to the inefficiency in parastatals, ineffectual infrastructure and problems of governance in general. The study sees a fundamental need to improve the enabling environment for private investment and the attitude towards private investment. The study presents two other themes, namely the need to arrest the deterioration of the environment and to promote regional integration.

To raise GDP growth in Africa to 4-5% per year, the investment ratio had to rise from 15% at present to 25% by year 2000. This depended on policy improvements and raising foreign aid to 10-12% of GDP. For the latter, ODA had to increase very significantly. A lower inflow of aid would imply either a lower target GDP growth at given efficiency levels or increased domestic savings. However, if a 4-5% per year output growth rate could not be achieved, it would lead to disillusionment and disappointment.

The Chairman queried the plausibility of the long term macroeconomic scenario put forward in the study. He also queried the realism of the assumption that ODA for Africa would increase at a faster rate than in the past, to raise Africa's share in total ODA. The Chairman invited the Committee to comment on the macroeconomic framework used in the study to underpin the foreign aid requirements.

A Committee member indicated that the measurement of efficiency through the use of the inverse of the ICOR was subject to error at different investment ratios. He suspected that the reported low rates of return to investment in Africa have reflected presently low investment ratios. Also there were many difficulties in measuring per capita income in Africa, given that many exchange rates were overvalued. Apart from the measurement issue, it was difficult to expect the regeneration of growth of real GNP of 3-4% per year in Africa from the current situation of adverse terms of trade and a generally unfavorable external environment. In addition, it was difficult to contemplate an inflow of foreign savings of 10-12% of GDP. In any case, if a country depended on that level of foreign savings, it could suffer Dutch disease effects. He felt that if adjustments were brought upfront, it was not necessary to have an inflow of 10-12% of GDP.

The Chairman suggested that the Region could consider an alternative approach to the present macroeconomic projections. He felt that it was better to pose the major issues of growth and then consider the different options for policy change and funding requirements.

Another Committee member raised an issue regarding the plausibility of aid inflow to Africa of 10-12% of GDP. This implied that the share of Africa in total ODA would increase rapidly. But significant ODA increases from major donors such as Japan and USA may not be forthcoming while most other major donors were already directing a large share of their ODA to Africa. The same committee member queried the macroeconomic scenario based on that funding assumption. He also felt that chapter 9 should take up the question of aid use, in particular the returns to investment using foreign aid.

The Regional staff explained that the aid estimates were not meant to be precise. They would adopt the options approach suggested by the Chairman, showing the dilemmas present in the current situation. They also emphasized that adjustment would be more difficult with limited funds.

A Committee member felt that the study should be careful in assessing the issues of limited ability of the governments to implement drastic change and the use of foreign aid. The Bank needed to concentrate on countries in which availability of resources could make a difference to performance. He also felt that the study should show how the new policies could increase efficiency and overall performance in individual countries.

Another Committee member felt that the problem of governance needs to be emphasized even more. He believed that the principal problem in Africa was the large size of the state. The tentacles of the State had spread all over these economies. The State was extracting rents and was contributing to inefficiency on a large scale as evidenced by the negative value added in many industries.

Yet another Committee member queried whether the Bank should be doing advocacy documents. He also represented a view that the rehabilitation of the infrastructure had to be emphasized and that more could be said about controlling population growth. The Committee member then raised several general issues regarding the study after noting the difficulties of doing a study on a continent rather than on a country. Nevertheless several issues needed to be analyzed adequately. He felt that the agriculture chapter had to be improved and the emphasis on human capital could be made stronger while the references made to corruption and military spending could be brought out more. He had a concern about the statistics used in the study but his staff would discuss this issue bilaterally with the Region. He also felt that the distinction between first and second generation strategies was overdrawn and he himself was not sure when one strategy ended and the other began. Perhaps the study could say what has happened in the last few years. He reminded the Committee of his earlier remarks on the exchange rate over-valuation and queried the somewhat negative statements on devaluation. He felt that the study's strong pitch for regional integration was counter productive and wondered whether the Region had thought adequately on this issue for Africa. In this regard, he asked whether presumed labor mobility was realistic, and how different industries were to be divided up among different countries. He believed that a focus on few countries or few regional arrangements such as the CFA zone would be more useful. He then raised questions about the informal sector. Did the Region know enough of the sector? In addition the Committee member suggested that the study should make a clear distinction between macroeconomic adjustment and structural adjustment. The Committee member suggested that the study could be issued as two documents. The first would be a more concise summary document dealing with the overall development strategy recommended by the study. It could receive wide disemination. The second document could be the revised version of the current study.

A Committee member questioned the approach taken in the study in terms of a single African macroeconomic entity. He said that equating a continent to a single macroeconomic entity would lead to fallacious analysis. Rather than take this global approach, he suggested a more selective and sectoral approach to defining the main problems and costing out the funding requirements. He cited examples for this from agriculture and education. He also felt that the Bank should not push for regional integration. Responding to the question on regional integration the Regional staff said that they would look at the framework for harmonization of policies, restructuring of utilities and merging industries across borders.

Another member raised several questions, regarding population growth, auction schemes for exchange rates, the role of expatriates, military versus social spending and whether the Bank had its own human resources to address these vexing questions. He complimented the Region for consultation with his staff on some of the legal issues in the study but expressed his disappointment at the very short notice given to members of the Committee before the discussion of this important paper. He also expressed the hope that ECA and OAU would be given a copy of the paper before its publication, so that their comments may be known to the Bank in advance and taken into account, if warranted.

A Committee member emphasized that what was important in the diversity in Africa for agriculture was not so much national boundaries as the different ecological zones. He felt that this diversity should be adequately addressed in the chapter on agriculture.

Summarizing the discussion, the Chairman suggested the study be revised to reflect the comments made by the Committee. He believed that the issue of diversity and the continental approach should be reconciled through better presentation. Rather than take a global approach, he suggested that the Region select a few themes that are important and consider policy options explicitly. He felt that the regional integration chapter was weak in defining ways of how to increase labor and capital mobility. He wondered whether there were practical ways of coordinating policies among 3 and 4 entities rather than take a global approach. He felt that the distinction between the first generation development strategy and the second generation development strategy was overdrawn. He asked that the study emphasize what governments were doing incrementally given an existing policy framework. While the study could not avoid dealing with the issue of financial resource requirements, the Chairman cautioned the Region to avoid pitfalls in the analysis. Above all the assumptions for projections had to be plausible. He felt that sufficient distinction had also to be made between equity and poverty alleviation objectives. The study should deal more with poverty reduction and food security.

The Regional staff will take into account the comments made by the Operations Committee and discuss the draft at the President's Council before holding an informal Board seminar.

July 14, 1989
SRajapatirana:gs

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: June 29, 1989

TO: Operations Committee

FROM: Vinod Dubey, Director, EAS

EXTENSION: 78051

SUBJECT: AFRICA: Long Term Perspective Study

The Operations Committee will meet on July 7, 1989 at 4.00 p.m. in Room E-1243 to discuss the Africa: Long Term Perspective Study.

Introduction

The Africa: Long Term Perspective study has been prepared over the last 2 years to take a view of Africa's development prospects beyond the current adjustment phase. An important feature of the preparation of the exercise was an emphasis on consultation with Africans and donors to identify the problems and define approaches for addressing them. The Region has obtained inputs from eminent Africans to build a consensus on the analysis of the issues confronting Africans and on feasible solutions. A yellow cover draft was completed in November 1988 and was discussed with representative of UN agencies, a broad group of Africans and donor representatives and with the Council of African Advisors. The Region indicates that a key feature of the preparation of the study was to develop an on-going process of consultation and partnership with African Governments and donor agencies that will continue into the implementation of the strategy following the publication of the study.

Relevance for Country Strategy

- The Region may wish to comment on this consultative and consensus approach to identifying the issues and solutions. Was the process helpful in strengthening the basis for future country strategy?

- Does the Region plan to use this approach to underpin a global strategy towards Africa? In the event, how does the "global" strategy translate to country specific programs and actions?

Data Issues

Given that the subject matter covered is necessarily wide and the period of review spans 30 years, data issues assume importance.

- The Region may wish to comment on the sensitivity of the analysis and conclusions to the availability and reliability of data beyond GDP, population and external accounts data.

- The Region may wish to comment on the issues of aggregation across countries and whether the conclusions are sensitive to the types of aggregation.

Analytical Issues

The Region may wish to comment on a number of analytical issues that arise in the study.

- the case made for group action and its compatibility with individual incentives (e.g. land rights of groups: Chapter 3)

- the distinction between strategies to achieve equity and poverty alleviation (Chapter 2)

- the case made for regional integration (Chapter 7).

Operations Committee

Messrs. Qureshi, Husain, Jaycox, Karaosmanoglu, Thalwitz
Rajagopalan, Fischer, Shihata, Wood, Vergin

cc: Messrs. Lee, Shakow, Holsen, Rao, Burmester/Thahane, Liebenthal,
Steer, Baudon, Hopper, Bock, Goldberg, Kavalsky, Parmar,
Pfeffermann, Baneth, Robless, Ms. Haug, Tanaka

SRajapatirana:gs

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THE WORLD BANK

Operations Committee

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Minutes of the Operations Committee to Discuss a PPR Paper on
THE ROLE OF FOREIGN DIRECT INVESTMENT IN FINANCING DEVELOPING COUNTRIES

Held on Friday, July 7, 1989, in Room E1243

Present

Committee	Others
Messrs. M. A. Qureshi, Chairman	Messrs. A. H. Gelb, CECFP
I. F. I. Shihata, LEGVP	J. A. Holsen, CECDR
S. Fischer, DECVP	J. Caprio, PPR
S. Shahid Husain, LACVP	G. P. Pfeffermann, CEIED
H. Vergin, OPNSV	M. E. Hinds, EMTTF
	I. Husain, IECDI
	D. R. Bock, DFS
	G. H. Reif, SPRPA
	F. Kilby, FRS
	F. Levy, EAS
	D. R. Weigel, IFC/MIGA
	A. T. Heron, CODOP
	D. M. Goldberg, LEGOP

1. The meeting was called to discuss a paper prepared by PPR as a companion piece for earlier Board papers following up the Brady Initiative. An agenda for the meeting was distributed by EAS.

2. At the invitation of the Chairman, PPR introduced the paper, explaining it had been requested by the Board. Among the issues treated are: (a) the potential importance of foreign direct investment (FDI) as a source of financing in the debt strategy; (b) the desirability of debt/equity swaps; and (c) the role of the Bank in encouraging FDI. As regards the first, it was concluded that FDI played an important developmental role - e.g., technology transfer - as well as financial risk sharing, in contrast to debt financing, and that it should be encouraged, but that it could not be expected to make a major contribution to filling the projected financing gaps of the heavily indebted countries. The report took a cautiously positive line with regard to debt/equity swaps, noting that there were both advantages and disadvantages that were to be weighed in the specific circumstances. Finally, the report describes in a general way what the Bank Group is doing to promote FDI but does not attempt to provide a detailed treatment.

3. On the first issue, there was broad agreement that the report had struck a proper balance on the usefulness of FDI and the role it can

be expected to play in the debt crisis. One speaker suggested that it was impossible to make a judgment on the usefulness of FDI in the abstract and that the paper should emphasize that the cost and benefit to the host country would have to be assessed in each case. Another speaker thought that the differences reported in the rates of return on equity investments and on debt were exaggerated and could be used as a reason to reject FDI, but other participants disagreed, finding that the differences were appropriate to the respective risks being taken.

4. There was also general agreement with the paper's emphasis of overall investment climate as the principal determinant of the level and efficiency of FDI, as opposed to the use of specific incentives. One member pointed out, however, that it is often the multinational corporations, rather than the host governments, that insist on special incentives, guarantees and protection from competition.

5. The Committee also agreed that a proper balance had been struck in the discussion of debt/equity swaps, one speaker commenting that it was one of the best discussions of the issue he had seen.

6. One member criticized the report as being too general in its treatment of a complex subject. He would have liked greater recognition that a lot of bad FDI had been carried out as well as good, and some analysis directed to the factors involved. He also noted the geographical (by source and recipient) and sectoral concentration of FDI historically, shifting over time, and would have liked to see some analysis of the reasons and the lessons to be learned. Moreover, the report made no mention of the evolving forms of foreign investment involving different contractual arrangements, portfolio investments, etc. Something should be said regarding their respective advantages and disadvantages, whether they should be encouraged, and how. He also believed that the treatment of what the Bank Group, including IFC, MIGA and ICSID were doing in this area was much too brief, and he thought attention needed to be paid to the possible coordinating role the Bank could play among the many international agencies that have been active in this area, including research and data collection.

7. The Chairman agreed that the report should take into account the wide array of new investment instruments available and the linkages that exist between the various forms of capital flow. It should also face the issue of bad investments, particularly since the reduction of other financial flows had greatly heightened the importance of FDI. In this regard, he agreed with the report's emphasis on host country policies as the principal factor in encouraging investment efficiency. He also pointed out the importance of industrial country policies in influencing the flow of FDI to developing countries.

8. Another member was concerned that the report did not respond to the expectations of the Board, insofar as it fails to suggest any action program for the Bank in this area. He shared the earlier speaker's opinion that much more needed to be said about what the Bank was already doing to encourage FDI and private investment in general. A number of speakers, including the Chairman, also expressed this view, noting that more should be said, with examples, about the positive impacts of

adjustment loans on the enabling environment for FDI and private investment generally (e.g., a new investment code in Mexico), innovative operations that encourage and provide a vehicle for private investment (e.g., a recent Pakistan energy loan), efforts in public enterprise restructuring and privatization and the increased attention given to this subject in CSPs.

9. The Chairman suggested that PPR undertake, in the context of its review of adjustment lending, an evaluation of whether adjustment operations were having a positive impact on the environment for private investment, including improvements of legal codes and regulations. Several speakers mentioned some studies already undertaken in this regard and offered to make them available.

10. Views were divided on the question of whether the paper should try to propose a specific FDI action program. It was agreed that giving a clearer picture of what the Bank is already doing would go a long way to conveying the direction in which it is moving. The Chairman suggested that the paper point to the positive impact on private investment, including FDI, of the initiatives begun under the private sector initiative, as well as the other activities pointed to in the discussion.

F.L.

FLevy:sb

July 12, 1989

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The World Bank/IFC/MIGA
O F F I C E   M E M O R A N D U M

DATE: 7-Jul-1989 11:04am

TO: Moeen A. Qureshi (MOEEN QURESHI)

FROM: David R. Bock, DFS (DAVID BOCK)

EXT.: 72942

SUBJECT: **FDI Paper for Discussion Today**

Moeen,

This is a good paper, but does not address the question that was implied in the US request, namely "is the Bank doing enough to promote FDI through the specific conditionality attached to its adjustment lending? What further lending instruments/conditionality should be developed in the context of Bank-Fund support for debt reduction?"

This isssue is not addressed at all in the paper, even implicitly. Worse, there is no discussion of the extensive adjustment lending work that is going on in a number of countries, and only brief mention of policy dialogue on this subject. MIGA and IFC get more mention than the Bank's adjustment lending.

I suggest you focus the discussion on Section VI, pages 15 and 16. This should be substantially expanded, and summarized in the introduction so that the Board knows that we are serious about promoting liberalized FDI regimes and sound macro policies to facilitate FDI flows. This paper creates precisely the wrong impression, namely that we know a lot about FDI but have marginalized it in our lending conditionality.

David

THE WORLD BANK / INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: July 3, 1989

TO: Operations Committee

FROM: Vinod Dubey, Director, EAS
V Dubey

EXTENSION: 78051

SUBJECT: Role of Foreign Direct Investment in Financing Developing Countries--Agenda

1. The attached paper was prepared by PPR as a companion piece for the earlier Board papers prepared by Bank staff as a follow-up to the Brady Initiative. The Committee may want to address the following issues:

Role of Foreign Direct Investment (FDI)

2. The paper concludes that FDI is important for developing countries as a source of technology, modern business practices, and access to export markets, but is unlikely to play a key role in the resolution of the debt crisis. Does the Committee believe that this represents a balanced assessment of the potential role of FDI?

Host Country Policies

3. The paper concludes that sound macroeconomic policies and stable and effective domestic economic management, especially as regards the climate for all private investment, are critical for the growth of FDI. Marginal, isolated changes in host country policies designed to provide special incentives to foreign investors are not likely to be very effective, and may be counterproductive. Host countries should, however, make efforts to reduce regulatory barriers that often impede FDI. Does the Committee accept this view of the relative role of general versus specific incentives for FDI?

Debt-Equity Swaps

4. The paper concludes that debt-equity swaps can, under certain circumstances (see esp. para. 31), provide a useful means of both ameliorating a country's debt problem and encouraging FDI. But the paper also stresses the potential negative effects of debt-equity swaps and calls for caution in the design and evaluation of such schemes. The Committee may consider whether this cautiously positive stance on debt-equity swaps is appropriate.

Role of the Bank Group

5. The paper briefly reviews the Bank Group's current activities directly or indirectly in support of FDI flows to developing countries. The paper does not call for a radical departure from current

practices. It recommends continued Bank support for improvements in the domestic business and investment climate, continued collaboration of IFC with foreign investors, continued build-up of MIGA, and funding of the FIAS trust fund. In addition the paper calls for increased Bank activity to upgrade investors' perceptions of developing countries, and to engage industrial country governments in a dialogue about their own policies regarding FDI flows to developing countries. Finally, the paper calls for close collaboration among staff from the various members of the World Bank Group. Considering that the paper was not designed to propose a detailed agenda for Bank Group support of FDI, the Committee may want to discuss where it appropriately reflects current Bank Group activities and direction in this area.

OC Members

Messrs. Qureshi, Husain, Jaycox, Karaosmanoglu, Thalwitz, Rajagopalan, Fischer, Shihata, Wood, Vergin.

cc: Messrs. Lee (COD); Shakow, Liebenthal (SPR); Holsen (CEC); Rao, Steer (FRS); Burmester/Thahane (SEC); Baudon (OPNSV); Hopper (PPRSV); Bock (DFS); Goldberg(LEGOP); Kavalsky (FRM); Parmar (CIO); Pfeffermann (CEI); Baneth (IEC); Robless (OPNSV); (Ms.) Haug, Tanaka (EXC); Linn (DECVP); I. Husain (IECDI); Gelb (CECFP).

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June 29, 1989

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THE WORLD BANK
OPERATIONS COMMITTEE

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Minutes of the Operations Committee to consider MALAWI: Agriculture Sector Adjustment Credit held on June 29, 1989 in Room E-1243

A. Present

Committee

Messrs. M.A. Qureshi (Chairman)
E. Jaycox (AFRVP)
W. Thalwitz (EMNVP)
F. Colaco (PREVP)
D. Goldberg (LEGOP)
E. Wessels (LATDR)

Others

Messrs. R. Ali (AF6AG)
R. Armstrong (AFRCE)
T. Baudon (OPNSV)
F. Chaudhri (EAS)
V. Dubey (EAS)
M. Fardi (SPRPA)
R. Grawe (AF6CO)
F. King (AF6CO)
Ms. K. Krumm (AF6CO)
I. Moreithi (AF6AG)
H. Messenger (AF6CO)
O. Storeng (FRM)
A. Zerabruk (LEGAF)

B. Issues

1. The meeting was called to discuss the proposals in Mr. Jaycox's memorandum of June 22, 1989 for an Agriculture Sector Adjustment Credit to Malawi. The discussion covered the main issues raised in the EAS's memorandum and some additional points.

Discussion

2. The Chairman opened the discussion with two observations: (i) most of the things the proposed operation is attempting to do are of long-term nature - not typically those to be supported by an adjustment operation. It was not, therefore, clear precisely what would be achieved through the proposed operation; (ii) the formulation and structure of conditions did not appear to be clear and monitorable in their present form.

3. Before discussing the focus of the proposed operation, the Region first described the broader perspective: the economy has been and continues to be subject to severe external shocks; high population growth is generating an excessive burden on limited resources and low agricultural productivity especially in the smallholder segment is keeping the living standards depressingly low. While most of the macro policies will be tackled in the context of the PFP, a critical central feature of the proposed operation, the Region stated, was to increase incomes of the smallholders. This will be done by allowing smallholders to grow the high value burley tobacco, popularizing the

use of fertilizer with traditional maize varieties (eliminating the fertilizer subsidy when the high yielding varieties - HYVs - become available for general use) by developing technical packages through improved research and extension and by efficient marketing arrangements.

4. A Committee member questioned the basic strategy to bring smallholders into the main stream which, in his judgment, would just 'freeze' the present group of smallholders as permanent smallholder with all the associated problems. He wondered whether consolidation of farms and encouragement of non-farm employment would not be a more useful approach.

Other Committee members raised several additional questions:

- Since tobacco producers are getting less than 1/3 of the auction price of tobacco, the question is why keep prices low on the one hand and give fertilizer subsidies on the other?

- On the merits of the policy content, can the proposed operation be treated as a sector adjustment operation?

- Keeping in mind the past performance, are the projections, especially of export growth, realistic?

- Since the three SALs to Malawi have not produced the expected results why are we doing an adjustment operation and not a regular sector operation?

- Are the credit and fertilizer subsidies consistent with the objectives of sustaining the budget deficit at a desired level and what will trigger the removal of subsidies?

- Does the government have an implementation capacity to administer these subsidies and how will the fertilizer coupon scheme work?

- Given the major issues in soil erosion, forest management etc. is the rather minor element (woodlots on tobacco estates) in the program an effective approach to the environmental issues?

5. At the Chairman's suggestion the Region first responded to the agriculture related issues. An urgent need in Malawi, the Region stated, was to achieve growth with equity. With local varieties of maize yielding only 0.6 tons/ha most of the smallholders were not even meeting their own food needs let alone generate cash flows for other uses. The use of fertilizer with local varieties has been shown to increase yields by 2 1/2 times and with hybrid varieties 6-7 times. Progress already made on the technical research side gives confidence that field tests can be done by end 1989 and more generally usable HYVs will be available within 2-3 years. The ratio of extension worker/farmer - 1:500 - was favorable compared with many countries and

the training-visiting (TV) system of extension was being introduced with promising results on a pilot basis.

6. In the Region's judgment, the single most far-reaching policy change in the current setting was to give smallholders the opportunity to grow high value burley tobacco which would yield gross returns 6 times higher than the next most profitable activity.

7. On environmental issues, the Region explained that sustained growth in agricultural productivity was absolutely critical because of the heavy population pressures on the land. With increased productivity, farmers would not be forced to cultivate the steeper slopes causing soil erosion.

8. The Region explained the factors that have kept tobacco prices low for producers: by doing so ADMARC has covered losses on its other crop accounts and its development activities. In the future, ADMARC will break even on its individual crop accounts and be reimbursed by the Government for its development activities. Tobacco producer prices are announced early in the year when actual auction prices are not yet known and as a result they have varied considerably as a proportion of the final auction price. In the future, ADMARC will institute a two-tier payment system which will increase the total return to farmers in years of high auction prices.

9. On the question of fertilizer subsidy, the Region felt that its removal now would substantially reduce smallholder production of maize, thereby necessitating imports which, given the relative fertilizer/maize prices, would cost substantially more foreign exchange. As the hybrid flint varieties become available to smallholders, the fertilizer subsidy could be reduced substantially. The Region also stated that subsidies will not increase the budget deficit because other lower priority expenditures will be adjusted downward to accommodate them.

10. In the Region's assessment, Malawi has a well-functioning civil service which can administer the pilot fertilizer coupon system within existing arrangements.

11. The Region was also confident that the country's basic commitment to structural/sectoral adjustment was sound but the refugee situation, transportation complexities/costs etc. were causing severe difficulties.

12. As to the long-term nature of the measures incorporated in the proposed operation, the Region stated that most of these are not new things - e.g. the strengthening of the extension system has been and continues to be pursued in other Bank operations. Certain key elements in the proposed operation - e.g. changing the land rent, the new policy on burley cultivation - make it an essentially a policy-based operation.

13. Towards the end, several Committee members expressed concern on the overall focus and the design of the program as a fast disbursing adjustment operation. The Chairman was especially concerned with the

lack of clarity and fuzziness in the statement of some conditions and the vagueness about the criteria which should act as a trigger for disbursement of second tranche.

Conclusion

14. The Region was authorized to appraise the proposed operation, keeping in view the concerns and observations expressed above. The Chairman stressed that the mission should pay careful attention to some worrisome macro issues e.g. exchange rate management; the operation should focus on key policy changes and clarify the monitoring of major conditions - explaining particularly the justification for the fertilizer subsidy; the rationale of the program as a sector adjustment operation has to be articulated; the program must have a good policy content and be seen as a full-fledged agricultural sector adjustment operation.

July 05, 1989
FMChaudhri:gs

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: June 27, 1989

TO: Operations Committee

FROM: Fred Levy, Acting Director, EAS

EXTENSION: 78051

SUBJECT: MALAWI: Agricultural Sector Adjustment Credit - Agenda

How much have SAL III achieved in SAL III ADMARC - problems

85/

tobacco growers getting only 30% of the price

The Region has distributed the Initiating Memorandum (IM) for the proposed Agricultural Sector Adjustment Credit (ASAC) to the Operations Committee with Mr. Jaycox's cover memorandum of June 22, 1989. The Committee is schedule to meet on Thursday, June 29, 1989 at 8.30 a.m. in Room E-1243 to consider the proposed operation involving an IDA Credit of US$60 million to be disbursed in two tranches.

Background

Despite three structural adjustment programs by the Bank and three standbys by the Fund since 1981, which have recently been reinforced by the IMF's ESAF and the Bank's Industrial Trade Policy Adjustment Credit (ITPAC) in 1988, Malawi has not been able to achieve expected levels of growth or make major progress in solving its structural problems. A major factor contributing to poorer than expected performance is reported to be slow growth in smallholder agricultural production. The proposed credit would attempt to realize smallholder agriculture potential by increasing the availability of improved technological packages, and to increase the degree of commercialization by strengthening the smallholder's participation in the input, output and credit markets.

The proposed credit would explore new vehicles to tackle some of the major constraints to agricultural development and poverty alleviation on a major scale with the goal of establishing a more productive and equitable agricultural sector. The proposed credit would support several actions, including developing new maize varieties; allowing smallholders to grow burley tobacco; ensuring adequate producer prices for smallholder tobacco; improving availability of fertilizer; halting land transfer from smallholder areas to estates; testing ways to target fertilizer subsidies, credit and other programs to the smaller smallholders; adjusting estate lease rates and establishing technical advisory services to them, and maintaining fertilizer subsidies at levels consistent with budgetary constraints and food security objectives.

Discussion Points

The Committee may wish to discuss the following points:

(i) Macroeconomic Context: Even though the second year PFP has been recently negotiated and an ESAF is in the offing, given the recurring nature of severe shocks that affect the Malawi economy, is the Region confident that appropriate macroeconomic policies, relevant to the agricultural sector - especially exchange rate adjustment, containment of inflation, enhancement of domestic savings - will be successfully implemented at the necessary scale and with the required speed?

(ii) Issues in the Proposed Operation

- The central thrust of the credit is to promote broad-based agricultural development by redirecting government policies and programs towards those smallholders who do not currently benefit from production incentives and agricultural services. Why is the proposed operation presented as a quick disbursing sector adjustment operation rather than as a straight investment operation.

- The IM gives the impression that smallholders can be brought into the main stream of agricultural activities by licensing them to grow the higher value burley tobacco, and by targeting fertilizer and credit to farmers with less than one hectare etc. How will it be possible to ensure that licensing and targeting will actually work to the advantage of the vast majority of the smallholders?

- Does not the proposed licensing/targeting approach involve great risks, particularly when the appropriate technology - e.g. suitable hybrid flint variety of maize - are likely to be available only after a substantial gestation period? What is the time frame for developing, testing and adopting the more desirable new varieties?

- Would not the administrative difficulties and costs (besides a high degree of leakage) required to cover several hundred thousand scattered farmers in the way it is proposed be extremely high?

- What proportion of the smallholders is now being serviced by the existing research/extention schemes and how much additional effort is needed to reach a majority of them?

- If estates are required to reduce the production of burley tobacco in order for smallholders to fill in the gap, would it not hurt export performance and economics of estate agriculture in the near future?

(iii) Fertilizer Subsidy and Adoption Problems

The IM seems to endorse the Government's intention to retain subsidies to encourage expansion of fertilizer usage, pending the development (and adoption) of a high yielding maize variety.

- Are such subsidies necessary and economically justified? How are they to be phased out?

(iv) The Shape of ADMARC

It is not entirely clear what roles, functions, objectives, structure and organizational features of the Agricultural Development and Marketing Corporation (ADMARC) need to be changed in order to streamline its operation. Could the Region explain the thrust of reform in the various aspects of ADMARC? In particular, how long would ADMARC take to pay substantially more than 30% of the auction price to the tobacco growers?

Operations Committee

Messrs. Qureshi, Husain, Jaycox, Karaosmanoglu, Thalwitz, Rajagopalan, Fischer, Shihata, Wood, Vergin

cc: Messrs. Lee, Shakow, Holsen, Rao, Burmester/Thahane, Liebenthal Steer, Baudon, Hopper, Bock, Goldberg, Kavalsky, Parmar Pfeffermann, Baneth, Robless, Ms. Haug, Tanaka, Agarwala Sandstrom, Messenger, Grawe

FMChaudhri:gs

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: June 22, 1989

TO: Mr. Moeen A. Qureshi, Senior Vice President, OPNSV

FROM: Edward Jaycox, Vice President, AFRVP

6/22

EXTENSION: 34000

SUBJECT: MALAWI - Agricultural Sector Adjustment Credit
Initiating Memorandum

1. The attached Initiating Memorandum seeks authorization to appraise in June 1989 a proposed Agricultural Sector Adjustment Credit to Malawi (ASAC), scheduled for Board presentation in December 1989. The proposed operation would involve an IDA Credit of US$60 million and estimated cofinancing of US$100 million. The draft Country Strategy Paper was circulated to the Operations Committee on June 20, 1989; the 2-page summary is attached for easy reference.

Background

2. Malawi experienced disappointing economic growth throughout the 1980's, despite the structural adjustment and stabilization program undertaking since 1981 with Bank and Fund support. Per capita income and consumption have declined, macroeconomic imbalances have persisted, and social indicators in health and education are among the worst in Africa. In addition to severe external shocks (especially regional security problems, highly variable weather, and weakening of terms of trade), a major factor contributing to poorer than expected performance has been slow growth in smallholder agriculture production. Further, the limited growth Malawi experienced in the present decade has bypassed most of the country's smallholders. They face chronic food deficits, which result in widespread malnutrition, and in one of the highest child mortality rates in the world.

3. The poor performance of the agricultural sector has been due to severe land shortages and low maize yields, which in turn are due to the lack of widely acceptable high yielding maize varieties and inadequate use of fertilizer. At the same time, the growth in estate output has declined as well, mostly as a result of ineffective utilization of land resources. In particular, smallholders with holdings of 1 ha or less are not served by the agricultural support services, and since they do not produce marketable surpluses, they do not benefit from market signals nor do they change their production decisions in response to them. These smallholders control a substantial proportion of the national agricultural resources, which they utilize at a very low level of technology. They are not effectively linked to the input and credit markets, and lack the financial resources to intensify their production.

4. The key sector in government strategy is smallholder agriculture, where the potential for increasing productivity is high.

The proposed Credit attempts to increase the availability of improved technological packages and to increase the degree of commercialization of smallholders by strengthening their participation in the input, output and credit markets. The proposed Credit thereby deals directly with those elements of agricultural production which contribute to their current poverty level.

The Adjustment Program

5. The Government implemented a broad-based structural adjustment program during 1981-1986 supported by successive agreements with the Fund and the Bank, comprehensive external debt rescheduling, and considerable external assistance. The Bank supported this program through three structural adjustment operations: SAL I in June 1981, coinciding with the second IMF Standby Arrangement; SAL II in October 1983, during implementation of the third standby arrangement and the extended Fund facility, and SAL III in December 1985. Substantial progress was made, in achieving macroeconomic balance, while quick-disbursing funds were provided to relieve balance of payments pressures and support private sector import requirements. In addition, project lending continued to support sectoral development and public investment programs. But the situation deteriorated rapidly during 1985-86 as a result of the external shocks referred to in paragraph 2 above. The Government undertook demand management and structural policy measures to improve the economic situation. The Bank supported these efforts through a supplement to SAL III in January 1987, which focussed on agricultural marketing reform. In February 1988, the Government formulated a three-year structural adjustment program (April 1988 - March 1991), which was supported by a three-year arrangement under the IMF's Enhanced Structural Adjustment Facility (ESAF) and by IDA's Industrial and Trade Policy Adjustment Credit (ITPAC). The program's major objectives are to achieve a high rate of economic growth, restore macroeconomic balances through continued discipline in the management of the exchange rate and fiscal and monetary policies, and implement key trade liberalization measures.

6. Implementation of the measures included under this decade-long adjustment and stabilization program has made good progress. Producer prices have been adjusted frequently. Balance of payments deficits have been reduced appreciably. Frequent tariff adjustments have allowed the major public utilities to remain solvent while restructuring of parastatals has reduced operating losses. An important achievement was the restoration of the fiscal discipline, resulting in a substantial reduction of the overall budget deficit. The Government's planning and budgeting process has been improved, although additional measures are needed to strengthen the key economic institutions. Actions have been taken to broaden the tax base while improving incentives, and to adjust exchange rates. Trade liberalization is proceeding as scheduled, with most intermediate goods and raw materials now free of controls.

7. The Bank and the Fund are currently completing the negotiations on the second-year PFP, which will provide the macroeconomic framework

33for the proposed Credit and for the second year of the ESAF and is scheduled for review by the Bank and IMF Boards in July 1989. In view of the effectiveness of the adjustment program during 1988 (preliminary indicators show improved economic performance in 1988, particularly in terms of increased income and consumption per capita), the macroeconomic objectives and strategies of the second-year PFP will remain largely unchanged from the first-year PFP with more emphasis on a rapid reduction in the inflation rate.

8. Improved management of the macroeconomic variables has contributed to the recent improvement in the economic situation. But even if successful in the short term, such improved macro-management requires concurrent improvements in management at the sector level, to increase medium and long-term production, productivity and income levels. The purpose of the proposed Credit is to support continued implementation of the macroeconomic reforms with intensification of improved sector management in agriculture. Particular emphasis would be placed on increasing smallholder productivity and on reducing poverty.

The Proposed Operation

9. The proposed Credit will be the next stage of the Bank's assistance strategy. Its main objectives are: (i) increased agricultural output and rural incomes, (ii) improved household food security, (iii) enhanced export earnings, (iv) reduced marketing costs, and (v) improved public resource management. On the agricultural and poverty side, the proposed Credit would support: shifting research policy and budget to develop high-yielding maize varieties; removing restrictions which prevent smallholder from growing high-value cash crops; improving availability and distribution of fertilizers; halting transfer of land from smallholder areas to estates; expanding the role of private traders; testing ways to target income generating activities to the poorest smallholders, adjusting land lease rents, and providing technical advisory services to promote efficient use of land resources on estates. On the macroeconomic side, the proposed Credit strengthens sound macroeconomic management in exchange rate, foreign exchange allocation, trade liberalization, price decontrol, and monetary and fiscal discipline (in the context of the forthcoming PFP) through essential balance of payment support.

10. The changes to be introduced under ASAC are supported by the IMF and the major donors, and are closely linked to the actions and investments they are supporting. The changes are also complementary to the adjustments pursued under the previous adjustment operations (particularly ITPAC, which shows a strong implementation record). Moreover, they complement the investment projects currently under implementation or proposed in the agricultural sector. These include the Agricultural Research, Agricultural Extension and Planning Support, Smallholder Credit, and Agricultural Marketing and Estate Development projects, and the proposed irrigation, agricultural services, and fisheries projects.

11. For the medium-term we envisage an agricultural sector where the decline in per capita maize production will have been arrested; the number of food deficit households will have been reduced significantly; smallholders will have managed to allocate more land for cash and export crops, and estates will have significantly improved efficiency in land utilization, thus increasing exports. The changes to be supported under ASAC would further this medium-term vision. In the short term, the implementation of the proposed Credit package would lead to increased production and reduced exports; in the longer term, to increased exports as well, thus strengthening the country's balance of payments. Production and welfare gains of the smallholder level are expected to outweigh the stabilization losses due to budget allocations for fertilizer subsidies. It must be kept in mind, however, that some of the envisaged measures may not show significant results during the Credit period (e.g.: research in maize). Others are innovative in nature (e.g.: targeted fertilizer subsidies), and there is no relevant experience elsewhere to help ensure success. Thus, the Credit would explore new ways of dealing with some of the major constraints to agricultural development and with poverty alleviation on a major scale, eventually leading to a more productive and equitable agricultural sector.

12. The proposed Credit would support a core of policy actions. These include developing new maize varieties; allowing smallholders to grow burley tobacco; ensuring adequate producer prices for smallholder tobacco; improving availability of fertilizer; halting land transfer from smallholder areas to estates; testing ways to target fertilizer subsidies, credit and other programs to the smaller smallholders; adjusting estate lease rates and establishing are estates technical advisory services to them, and maintaining fertilizer subsidies at levels consistent with budgetary constraints and food security objectives. Additional measures to be supported by the credit would complement these core action and enhance their impact.

13. The proposed Credit is explicitly designed to address the needs of the poorest among the rural population. Most of its features would increase their income and enhance their food security. The adoption of geographically differentiated maize prices, however, may reduce producer prices and increase consumer prices for considerable number of people. The proposed Credit would thus include an SDA (Social Dimension of Adjustment) component, currently under preparation by a Bank mission, to strengthen the local capability to monitor and analyze the socio-economic impact of the adjustment program and to fund pilot schemes to protect the most vulnerable groups.

<u>Status of the Policy Dialogue</u>

14. All the issues addressed in the Initiating Memorandum have been discussed with the Government and a broad degree of agreement has been reached on the core program described in paragraph 12 above, which is already reflected in Government's Statement of Development Policies, 1986-1996. Some disagreements remain on procedures for targeting burley tobacco licenses, and food and fertilizer for work schemes to the poorer

smallholders, and the remaining details will be worked out at appraisal. A few areas, which are not part of the core program, remain controversial and will be resolved at negotiations. They are the adoption of geographically differentiated fertilizer and maize prices, the balancing of each ADMARC's crop accounts, and procedures for targeting fertilizer subsidies to the poorer smallholders. The Initiating Memorandum has been discussed with IMF and there are no differences of views over the period of the next PFP and the Credit's implementation period. In the medium term, we have agreed with the IMF to revisit the issue of the level of fertilizer subsidies. The IMF would like to restrict the subsidies to less than 1% of budget expenditures while we estimate that by 1992/93 allocations equivalent to 2.5% of budget expenditures would be required to achieve the intended production and equity objectives.

Attachment

DISTRIBUTION:

Operations Committee Members	Messrs. Karaosmanoglu (ASIVP); Thalwitz (EMNVP); Husain (LACVP); Wood (FPRVP); Shihata (LEGVP); Rajagopalan (PREVP); Fisher (DECVP); Vergin (OPNSV)
Other Attendance	Messrs. Lee (CODDR); Dubey (EASDR) (2); Shakow (SPRDR) (2); Holsen (CECDR) (3); Rao (FRSDR) (2); Burmester/ Thahane (SEC); Liebenthal (SPRPA); Steer (FRS); Baudon (OPNSV)

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SUMMARY AND CONCLUSIONS

i. The Problem. Malawi presents an apparent paradox: during most of the 1980s it embraced an adjustment and development strategy guided and supported by the Bank and IMF, but its economic performance has been disappointing. Per capita income and consumption have declined, macroeconomic imbalances have persisted, and social indicators have remained extremely low, even by African standards. These poor results have arisen from two factors: the impact of severe external shocks (especially regional security problems) on a fragile and resource-poor economy; and rigidities in the political and social system. In retrospect, Bank assistance strategy in the 1980s underestimated the depth of Malawi's structural rigidities and the limitations in implementation capacity.

ii. Malawi enters the next decade facing some daunting development problems: the population growth rate is one of the highest in Africa and is creating a massive demand for food, energy, and social services; smallholder agricultural productivity is declining and more than one-half of the rural population faces seasonal food deficits and low nutrition levels; the country has relatively undeveloped human resources, with exceedingly poor education, literacy, health, and mortality levels; poverty is worsening and income differences are widening; the young and fast-growing labor force is putting pressures on labor market absorption; population growth and the refugee influx are creating severe pressures on the environment; and the limited export base is making Malawi extremely dependent on balance of payments support.

iii. Government Development Strategy. The Government prepared a comprehensive new medium-term development strategy in 1987. We support the broad thrust of this, especially the emphasis on smallholder agriculture and the recognition of distributional, human resource and environmental problems. However, there are several areas where we believe current policy to be inadequate: population issues are weakly addressed; there is insufficient attention to poverty alleviation; short-term stabilization is over-emphasized at the expense of medium-term growth; public expenditures emphasize capital investments over recurrent financing, and infrastructure over human resources; and there is lingering mistrust in Government of private sector decision-making, in particularly with respect to the Asian entrepeneurial class.

iv. Macroeconomic prospects. Successful implementation of the Government's development strategy could lead to medium-term growth of five percent. A large transitional import surge will be necessary in 1989-90 to support recovery from the severe import compression of the 1980s and provide for increased agriculture-related imports, especially of fertilizer. While export proceeds will provide an increasing share of Malawi's foreign exchange resources, current account deficits of the order of nine percent of GDP in 1989-91 declining to six percent in the mid-1990s are projected. A large inflow of concessional external funds is required to finance these deficits and Malawi will continue to depend on adjustment financing flows under the Special Program of Assistance and follow-on programs at least to the mid-1990s.

v. Bank Assistance Strategy. Our goal is to provide effective support in the following four areas:

- Restoring growth. Our primary focus will be on tackling the problem of low smallholder agricultural productivity. The focal point of our work will be the fast-disbursing (FY90) Agricultural Sector Adjustment Credit (ASAC) that will support liberalization of the sectoral policy framework. We will also support the completion of import liberalization, financial sector development and the development and maintenance of economic infrastucture.

- Tackling long-term development issues. We are increasing allocations to investments in education, health, and skills training. In population, we will be continuing an activist position on family planning. In environment, we will continue to address deforestation and land degradation problems in economic work and project lending. We will focus on women's access to agricultural technology, social and credit services and will prepare a WID Strategy Paper in FY90.

- Poverty alleviation. We are launching a number of studies to support the development of a comprehensive poverty strategy, including the FY90 Country Economic Memorandum, the FY90 Food Security Report, and Social Dimensions of Adjustment research. This work will feed into sector lending, ASAC, and the FY91 poverty-oriented adjustment operation.

- Macroeconomic management. We will continue to work with the Fund and the Government in developing a macroeconomic framework that balances stabilization objectives with growth requirements. Working relationships with Fund staff have generally been good, but we have encountered substantive and procedural problems in the PFP process, including disagreement over the level of public expenditures. We plan further analysis in the follow-up to the FY89 PER and in an inflation research project being undertaken in collaboration with the Government.

- Public sector management. We will support institutional strengthening of government agencies through a FY89 project and technical assistance under the PER, followed by a comprehensive review of PSM issues in FY90-91. This will be complemented by parastatal reform.

vi. Operational Implications. We recommend:

- A lending program equivalent to US$13 per capita in IDA-9, compared with US$11 in IDA-8, with 40 percent in adjustment operations;

- An annual increase of 5-10 percent in CAM resources for the next two to three years to strengthen the pipeline, sharpen the policy content of operations and allow more work on programs of special emphasis;

- Financing an increased share of development-related recurrent expenditures, in line with the recommendations of the FY89 PER; and

- Financing up to 95 percent of total project costs, in view of the Government's tight budgetary position and limited revenue base.

vii. Risks. The country strategy reviewed here faces a number of risks, including deterioration in the external environment, policy slippage, and inadequate external financing. We propose that deterioration in the external environment or underfunding would trigger increased IDA flows, if policy progress remains strong, while serious policy slippage would lead to a suspension of adjustment and related operations, leading to a cut in commitment levels of about 50 percent.

June 26, 1989

2.

CONFIDENTIAL

Minutes of the Operations Committee meeting to consider TANZANIA: Agriculture Adjustment Program- IM held on June 26, 1989 at 3.00 p.m. in Room E-1243

A. Present

Committee

Messrs. M.A. Qureshi (Chairman)
E. Jaycox (AFRVP)
W. Thalwitz (EMNVP)
R. Steckhan (LA2DR)
O. Yenal (ASIVP)
H. Scott (LEGVP)
J. Wood (FPRVP)
F. Colaco (PREVP)
H. Vergin (OPNSV)

Others

Ms. E. Adu (LEGAF)
R. Ali (AF6AG)
R. Armstrong (AFRCE)
T. Baudon (OPNSV)
F. Earwaker (SPRPA)
R. Grawe (AF6CO)
D. Kaufman (AF6CO)
F. Levy (EAS)
H. Messenger (AF6CO)
G. Nkojo (AF6CO)
J. Olivares (AF6AG)
A. Ray (EAS)
V. Srinivasan (AF4PH)

B. Issues

1. The Operations Committee met on June 26 in Room E-1243 to consider the Initiating Memorandum on Tanzania - Agriculture Adjustment Program. The discussion followed the agenda prepared by the Economic Advisory Staff,

C. Discussion

2. In its opening remarks, the Region said that since the introduction of the Economic Recovery Program substantial progress in economic adjustment has occurred; in particular per capita GDP has grown in real terms. The Bank is now encouraging privatization while continuing to support improvements in public sector management. The two main structural weaknesses that need to be addressed at this time are in the financial sector and in agricultural marketing. Preparatory work for a financial sector operation has started. This credit would enhance the efficiency of agricultural marketing and processing, rationalize input supply systems and eliminate non-economic parastatal investments and operations. Its macroeconomic linkages would be very direct, for example it would help eliminate marketing board losses that have been a major contributor to inflation.

3. The Chairman raised the question of taxation in agriculture: would a system of agricultural taxation be appropriate once the system has been cleared up? The Region said that at this time there is a large amount of "implicit" taxation due to parastatal marketing inefficiencies so that additional taxation is not the issue, but studies are underway to define a broad tax reform program. The

Chairman enquired about the transition to free markets, which he felt was the central design issue. In response the Region said that in view of the poor experience with price stabilization schemes elsewhere it does not see the need to safeguard the transition through price guidelines or stabilization schemes. This would militate against the objective of reducing the role of the Government. The Chairman agreed that many price stabilization schemes have not worked, but suggested that further consideration might be given to reviewing other experience on this issue, especially on variable export levy schemes.

4. A Committee member questioned whether Tanzania could afford to raise producer prices. Other questions referred to the case for grain reserves, pricing of fertilizers, support services, disbursements and the viability of creating competitive auction markets. The Region reiterated the heavy implicit taxation from which farmers have been suffering(with producer prices constituting one of the lowest shares of international prices in East Africa). Parastatal inefficiencies are currently so large that sizeable increases in producer prices and reductions in parastatal losses would be expected to result from the major marketing restructuring envisaged under the proposed operation. In the case of grain reserves, the Region said that the operation of this buffer stock is essential for food security reasons, particularly given the foreign reserve position of Tanzania, but it also agreed that it should be supplemented by appropriate foreign currency reserve management, so as not to rely exclusively on only one method. Regarding the domestic price of fertilizers, the Region felt that the nature of foreign aid which currently supports fertilizer is fungible, and hence the opportunity cost would be the free world price. The Chairman stressed the need for generating additional revenues in agreeing that the fertilizer price ought to be raised.

5. On the provision of support services to supplement the various institutional changes being proposed in this credit, the Region mentioned a number of operations that are being prepared to improve infrastructure and credit. Regarding the disbursement mechanism, the Region said the list is wide although it is not a negative list. It noted however that although as a percentage of the total value of imports, the OGL is not very large at present, by the end of the year it is expected to include most categories and types of items imported by Tanzania except for a small negative list. Finally, with respect to auction markets, the Region noted that the state of preparedness varied by crop but there were no alternative ways to proceed.

6. In conclusion the Chairman reiterated that the proposed operation promises to be a very good one and strongly expressed his support.

July 03, 1989
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THE WORLD BANK

Operations Committee

CONFIDENTIAL

Minutes of the Operations Committee to Consider
NIGER - Education Sector Adjustment/Investment Project Initiating Memorandum

Held on Monday, June 26, 1989, in Room E1243

A. Present

Committee

Messrs. M. A. Qureshi, Chairman
E. V. K. Jaycox, AFRVP
W. P. Thalwitz, EMNVP
H. N. Scott, LEG
F. X. Colaco, PREVP
B. G. Kavalsky, FPR
G. Tidrick, ASI
R. B. Steckhan, LAC
H. Vergin, OPNSV

Others

Messrs./Mmes M. J. Gilleltte, AF5DR
V. Dubey, EAS
A. Rigo, LEGAF
F. L. Laporte, AF5DR
S. J. Ettinger, CODOP
B. J. Fredriksen, AF5PH
G. P. Sicat, EAS
M. W. van Eeghen, AF5CO
R. Clement-Jones, AF5CO
P. J. Dufour, FRM
G. N. Swamy, AFRCE

B. Issues

1. The Committee followed the agenda prepared by EAS. The discussion centered on the nature of hybrid operations, especially as applied to the social sectors. This led to a set of interrelated issues in the link between adjustment and investment credits and the justification for quick disbursing components.

Issues of Credit Design

2. The Chairman asked the Region to introduce the topic by addressing three issues: (a) why a quick disbursing credit design utilized a hybrid design instead of a SAL vehicle; (b) whether there is a budgetary and a balance of payments counterpart in the project which needed to be financed; and (c) whether the structure of the Credit is related to co-financing constraints or opportunities available to IDA.

3. Choice of Hybrid Design. The Region stated that Niger had undertaken a SAL about three years after the Fund's initial intervention in 1982, followed by a public enterprise sector adjustment project (PESAP), which is still being executed. The third and last tranche of the PESAP has not been released as the Government has been having difficulty in handling the full range of reforms envisaged. Thus, progress towards a second SAL operation would be more difficult because this instrument requires more comprehensive actions. The political

environment is shaky. The new president is still establishing popular support after sweeping into power upon the death of President Koutche - the real architect of economic reforms. Thus, political constraints are holding back actions that would be required by a SAL. However, the Region is undertaking selective interventions on reforms in the country. The proposed operation in the education sector is designed to introduce key reforms to improve efficiency and effectiveness of resource use. Because the export of workers is important to Niger's economy, education absorbs a large proportion of the country's current budgetary resources. The hybrid format would support the deepening of the reform process within the sector by bringing about a tighter working relationship between the Education Ministry with the Ministries of Finance and Plan.

4. The Region further said that the sector investment program had been made to fit the sector adjustment program, as it were, like "hand-in-glove". The hybrid format, instead of two separate operations, would result in a considerable saving in Regional staff and budget resources.

5. Budgetary and Balance of Payments Counterpart. The Region stressed that there is a budgetary linkage with the quick disbursing money; it would generate CFA resources to be used in the budget. The sector reforms increase the demand for budgetary uses in education, in the context of a tight budgetary situation. The overall budget situation would be governed by the ESAF program with IMF.

6. The Region further stated that the budgetary gap would exist so long as the balance of payments gap existed. There was a persistent stagnation in revenue due to the shift of economic activity from the formal to the informal sector due to the overvaluation of the CFAF exchange rate. The country has a large debt service. A narrowing of the balance of payments gap could be helped by debt relief and by a CFAF devaluation. The economy, however, has not realized much supply response to adjustment measures even though the Region observed some vibrancy in the informal sector. The situation had been aggravated by the recent devaluation of the Nigerian currency which has encouraged informal sector imports into Niger from Nigeria which further aggravated the payments gap.

7. Burden-sharing Opportunities. The Region stated that opportunities for additional SPA resources are available for the operations. Of the proposed US $20 million proposed as quick disbursing component, $18 million is expected to be financed by SPA. In addition, about $12 million of co-financing is expected for the investment component. Thus, IDA could help to leverage a lot of additional external funds.

8. The Issue of Quick Disbursing Money Against a Negative List. A member argued that the use of a negative list in the disbursement of the quick disbursing component would require a stronger justification which should be valid across the other Regions.

9. The Region replied that, in this case, they had several objectives. The PFP process involved the Bank with a gap filling exercise which needed the negative list approach. Since it would take quite a while to produce a SAL operation, there was no vehicle to get

the funding across (paras. 3 and 6). Besides, the quick disbursing component to be provided by IDA would only be 10% of the total.

10. Issue of Linkage Between Investment and Adjustment. A member asked about the objective tests or "organic link" in moving from project to hybrid operations. There was no balance of payments justification because he did not find an adverse terms of trade situation for the country that needed to be financed. The budgetary argument was not clear since total budget expenditure was predicted to be higher than public educational expenditure. He asked whether a quick disbursing operation would be justified whenever co-financing resources are available. In short, where was the litmus test as the operation progressed from project to hybrid that would allow IDA to draw the line? He suggested that perhaps there was a lack of credit vehicles that countries could qualify for.

11. The Region replied that the hybrid concept must have a recognizable integrity. That vehicle could be used in order to attract high level Government attention to important development issues, for instance, in this case, the budgetary problems caused by the Government's current policy of pre-recruiting most students to civil service jobs at the time they enter the university.

12. The Region also indicated that the issue of "organic link" between investment and adjustment could be overdone and is not practical. Many cases could happen that would justify the hybrid concept and it is important in such cases to seize the opportunities.

13. Hybrid Credits in the Social Sectors. The Chairman summarized the Region's major arguments in favor of the use of a major sector operation to justify the need for quick disbursing money. Yet, he expressed his concerns. He said that in the Bank's Adjustment Lending Paper, macro-conditionality for quick disbursing money is used to support economic adjustment with balance of payments assistance and does not make a distinction on the method of disbursement as to positive or negative list. He said that the policy concept of quick disbursing money in social sector operations is murky. It is difficult to devise conditionalities that are precise, objective and monitorable. For instance, it is difficult to judge objectively the "satisfactory" implementation of teacher training. He therefore felt that tranche release conditions should be carefully and precisely worded. As a sector investment project, he found the proposed operation as a good example of an investment project. IDA has done education projects for the last 15 years, but these have been made without any quick disbursing money.

14. The Chairman further distinguished the differences with sector credits in directly productive sectors with quick disbursing money in which the balance of payments link could be clearly found. This is easily established, for instance, in sector loans in industry and trade involving import liberalization. In agricultural sector adjustment credits, quick disbursing money is made available for the import of agricultural inputs like fertilizers and insecticides; this incidentally, is a disbursement against a positive list of imports. The link to the balance of payments need therefore has no generic

distinction as to a negative or a positive list for import disbursements. In the social sectors, such a link is hard to establish. For instance, it is difficult to find a connection to the balance of payments in providing more books for the people or in having more women in school.

15. Some members felt that establishing the balance of payments link for the social sectors is not essential. One member stated that so long as the macro-economic program was in place, it is not critical to establish the adjustment-investment link. Another member felt that the linkage between conditionality and the investment side is not an easy task. In both instances, the members praised the high quality of the operations and the good design of conditionality.

16. The Region recounted that hybrid operations in the productive sector began initially with the concept of sector structural adjustment operation (SECAL) with quick disbursing money; the investment project component was added to the SECAL. In the case of social sectors, the Region indicated that they started with a sector investment project and then linked this with the need to fill the macro-economic and budgetary gaps. The Region argued that both these concepts are valid approaches to the formulation of the hybrid operation.

17. The Chairman concluded that the Region could go ahead with the operation as proposed but that they should keep in mind that there is a considerable discomfort with applying the hybrid operational concept in the social sectors. He felt that it is part of the apparatus of support to client countries to devise credit vehicles that seek leverage with other co-financing donors.

18. The Chairman also said that no distinction need be made between sectors for purposes of qualifying for quick disbursing assistance. However, it would be important to be as selective as possible in applying the hybrid Credit concept to the social sectors.

<u>Sector Issues</u>

19. A member asked how committed the Government is to undertake binding reforms in the sector. He indicated that some reforms are very difficult to pursue and he preferred therefore that these policy reforms be front-loaded rather than made as conditions of the tranche release. The Region stated that there is now quite a lot of front-loading in the actions of Government within the civil service and in the education sector. These actions show good commitment to reforms in the sector by the Government. However, the Region recognized that many of the reforms are politically sensitive and could pose implementation problems. These aspects would be given special attention during appraisal.

<u>Decision</u>

20. The Committee gave the Region permission to appraise the proposed Credit in accordance with the Initiating Memorandum.

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July 5, 1989

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The World Bank
OPERATIONS COMMITTEE

CONFIDENTIAL

Minutes of the Operations Committee meeting to consider the FY88 Country Strategy Paper Review, held on June 26, 1989 in Room E-1243.

A. Present

Committee	Others
Messrs. M.A. Qureshi, Chairman	Messrs. J. Bock, DFS
E. Jaycox, AFRVP	F. Earwaker, SPRPA
I. Shihata, LEGVP	S. El Serafy, EAS
W. Thalwitz, EMNVP	T. Hutcheson, SPRPA
H. Vergin, OPNSV	D. Lee, COD
J. Wood, FPRVP	F. Levy, EAS
J. Linn, DECVP	R. Liebenthal, SPRPA
N. Roger, LACVP	D. C. Rao, FRS
O. Yenal, ASIVP	A. Shakow, SPR
	A. Steer, FRS

1. The meeting was called to consider a paper, prepared by the Strategic Planning Review Department of PPR, reviewing experience with CSPs during the first fiscal year subsequent to the reorganization of the Bank. An agenda for the meeting was prepared by EAS.

B. Issues

2. At the invitation of the Chairman, PPR made an introductory statement. It said that the paper has stimulated a lot of discussion, and a sequel to it was due in the near future, to cover FY89. Actions have already started in harmony with the paper's conclusions, but not necessarily in reaction to it. For example, decisions have been made to firm up the scheduling of CSPs; to ensure proper coverage of risk management in the strategy papers; to encourage greater realism in the projections; to define more clearly the triggers that would activate alternative program scenarios. The notion of an Initiating Memorandum (IM) to launch the CSP seems also to have been accepted. What perhaps remained to be agreed, PPR added, is how to evaluate trigger mechanisms for the scenarios elaborated for the heavily indebted countries. Finally, PPR highlighted several issues to be considered by the OC: namely, defining the CSP audience; correcting the perceived imbalance between macroeconomic and sectoral analysis in many CSPs and in the review process; improving the realism of CSP projections; and defining the comparative advantage of the Bank in a particular country context. Indicating sector priorities is another topic worthy of discussion, though further work obviously needed to be done on this.

C. Discussion

3. The Chairman began by enquiring when the last CSP guidelines were issued. EAS said that guidelines had been issued in January 1987, and later revised after the reorganization and issued as an Operational Manual Statement in July 1988. COD added that this OMS would be revised again shortly, to be issued in the new series of Operational Directives. The Chairman said that he thought the lack of adequate sectoral coverage in CSPs was true for some, but was not typical, and invited comments on CSP coverage and the issue of realism.

4. A member said that encyclopaedic coverage, if pursued, would lead to loss of strategic focus, and that he was averse to the CSP getting into sectoral details. While such details were essential for the staff, they were not appropriate for senior management decisions on country strategy. Another member added that the CSP as a document was not the same as the CSP as a process, the latter seeking to build consensus during the working level and Regional Vice President reviews, so that when the paper came to the OC it sought approval for plans already made and guidance on major strategic choices. At the OC stage, the Region should not be inhibited from seeking guidance on strategic options. The issues covered in the CSP could be macroeconomic or sectoral, depending on the particular country situation.

5. Another OC member thought the guidelines on CSPs should be clear on the respective roles of the Regions, PPR, EAS and Finance in the CSP process, and thought that members of the Legal Department should be involved in the process. He stressed the need for coordination on risk management. Referring to para. 45 of the paper, he saw scope for useful Bank lending, for example in the social sectors, which did not hinge on pre-conditions of macroeconomic reform. He thought that CSPs should clearly identify the issues that need to be decided by the OC, so that clear decisions are elicited rather than leaving matters undecided at the end of an OC meeting.

6. A member noted that the present guidelines highlight a set of mandatory checkpoints to be covered, such as country risk analysis and burden sharing, which ensure that institutional concerns and priorities are focused on. Forcing coverage of all or particular sectors, however, is often seen by Regional staff as making the CSP an advocacy document for Divisional lending programs and limits the choice of strategy options. He liked the distinction made by a previous speaker between the document and the process.

7. The Chairman expressed the view that the fundamental purpose of the CSP was to get management guidance regarding the framework in which the country policy dialogue would be conducted and the lending program developed. He recalled that the same issues were raised with the same reactions when CPPs were initiated. He shared the view that the encyclopaedic approach, attempting to cover all sectoral and other concerns, would take the CSP in the wrong direction. The strategic focus of the CSP is crucial and, for that purpose, the document should be lean and selective. At the same time, there would be countries for which the main issues were sectoral rather than macroeconomic.

8. One speaker noted that it is not always clear what management at the different levels should decide: is it the trigger points determining different program levels, or is it resource allocation within the program? Another speaker suggested that this could be clarified in each country case by the use of the recommended IM for CSPs. Another speaker disagreed, however, saying that this top-down guidance is being achieved through the previously mentioned mandatory checkpoints. Top management could not be expected to decide specific country issues in advance. In any case, the major resource implications of different assistance scenarios needed to be spelled out in the CSPs.

9. The Chairman said it was incorrect to think of the CSP as a top-down process. Senior management cannot indicate country development needs, which are best identified by staff working on these countries. He could not himself substitute for the country Division Chief who, familiar with a country situation, should initiate the strategy to be reviewed at various stages in the process until it reaches senior management. It was advantageous to have a standard format and general guidelines to be followed. The result is not always ideal, but it works; and it is true that when circumstances are fast changing, the CSP may need updating. He remained convinced, however, that the coverage should be selective and that this should properly be left to Regional management to decide.

10. As to realism, the Chairman asked if Committee members agreed with the paper that the projections have been unrealistic. The natural optimism of country officers is usually tempered by the Financial Complex concerns over the portfolio, and he himself thought that having these different perspectives was healthy.

11. A member denied that CSPs were chronically optimistic. He failed to see any lack of realism when creditworthiness was discussed. The Chairman said the contention was that Operations' staff tended to overestimate country prospects and made overoptimistic forecasts of capital inflows. This process, it was suggested, resulted in overestimating future economic prospects, including such things as prospective growth rates. "Was this criticism valid?" He asked. The same member said that we seemed unable to forecast commodity prices correctly. Another said he thought that the actual outcome tended to fall short of the projections. Yet another member added that the future would always be uncertain. But the Chairman insisted: do we collectively have an upward bias? There was little consensus on this issue. A member said that the issue was not one of unrealistic projections but rather of normative projections that led to misjudging the probabilities of different outcomes. Another asked why projections were considered a major issue, inasmuch as decisions were made on the basis of actual situations rather than on the projections made in CSPs.

12. The Chairman expressed his personal view that it was not correct to suggest that Operational staff growth projections were consistently overestimated or unrealistic. He could see the problem more clearly in the context of Bank-Fund collaboration, particularly on PFPs. Bank's estimates for the financial gap tend to be larger than those of the Fund because the Bank is usually pushing for a greater flow of external financial support in order to ensure a minimum growth rate in the economy. This might not always work, but it would be wrong to say that the Bank's projections tended to be more unrealistic than, say, those of the Fund. He also noted

that the external environment had a great deal of influence on the realism of the projections. During periods when the external environment had been favorable, Bank's operational projections were found to be pessimistic. However, in the recent past, when the external environment had been quite bleak, it was understandable that the Bank's projections appeared overoptimistic.

13. As the discussion ended, the Chairman thanked PPR for producing such a stimulating paper.

July 10, 1989
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THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: June 20, 1989

TO: Operations Committee

FROM: Vinod Dubey, Director, EAS

EXTENSION: 78051

SUBJECT: FY88 Review of Country Strategy Papers

The Operations Committee will meet on June 26, 1989 at 4.00 p.m. in Room E-1243 to discuss the paper FY88 Review of Country Strategy Paper.

Issues

The Committee members may wish to focus on the following issues in their discussion:

The Audience

- Who is the primary audience of the CSP? Is it to be considered as a document the preparation of which helps develop a consensus among staff on the appropriate assistance strategy for a country or as a document through which management guidance and approval on such a strategy is obtained?

CSP:/

Triggers Points.

The Content

- Should there be a mandated balance in the strategy discussion between macroeconomic and sectoral issues? Is there an over-emphasis on macroeconomic issues compared to sectoral issues?

- Alternatively, should the macroeconomic and sectoral balance of the strategy discussion be left to the discretion and expertise of the Region.

How can we have more attention to Sectoral Issues. Change the balance to some extent

Realism

- Is there an overall tendency to be optimistic about country projection? How do CSP projections compare with other Bank projections including those in country reports, WDR and long-term prospects and commodity forecasts prepared by PPR?

- What is the appropriate approach to increase the realism of the CSP projections? Should this be done at working level reviews through effective participation of staff from the global forecasts producing departments and Finance or should the realism be ensured via other means? (for example a framework to check consistency, and explicit statements of underlying assumptions.)

What should the Bank be doing, less of [illegible] [illegible]

. Is there a need to mandate specific ways to evaluate country risks in CSP over and above recent instructions? How best is this to be accomplished?

<u>Review Processes</u>

. Is there a need to strengthen the present review processes? In particular, should the initiating process for CPPs receive greater attention?

. Is the current review process cost effective in terms of time and effort?

<u>Operations Committee</u>

Messrs. Qureshi, Husain, Jaycox, Karaosmanoglu, Thalwitz, Rajagopalan, Fischer, Shihata, Wood, Vergin

cc: Messrs. Lee, Shakow, Holsen, Rao, Burmester/Thahane, Liebenthal Steer, Baudon, Hopper, Bock, Goldberg, Kavalsky, Parmar, Pfeffermann, Baneth, Robless, Ms. Haug, Tanaka,

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THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

Mr. Qureshi
E-1241
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DATE: June 21, 1989

TO: Operations Committee

FROM: Robert B. Liebenthal, Acting Director, SPR

EXT: 34696

SUBJECT: FY88 Review of Country Strategy Papers

An Operations Committee meeting will be held on Monday, June 26 at 4:00 p.m. in Room E-1243 to discuss the attached FY88 Review of Country Strategy Papers. An agenda will follow shortly.

Attachment

Operations Committee
Messrs. Qureshi, Husain, Jaycox, Karaosmanoglu, Thalwitz, Rajagopalan, Fischer, Shihata, Wood, Vergin

cc: Messrs. Lee, Dubey, Shakow (o/r), Holsen, Rao, Burmester/Thahane, Steer, Baudon, Hopper, Bock, Goldberg, Kavalsky, Parmar, Pfeffermann, Baneth, Robless, Ms. Haug, Tanaka, Aguirre-Sacasa

FY88 COUNTRY STRATEGY PAPER REVIEW

May 5, 1989

Strategic Planning & Review Department
The World Bank

COUNTRY STRATEGY PAPER REVIEW

Table of Contents

Thanks are due to numerous staff and managers who shared their experiences freely

A. INTRODUCTION

(i) Purpose of this Report

1. The aim of this paper is to review the Country Strategy Papers (CSPs) prepared in FY88 to see how they, and the process of their preparation, contributed to the development of the Bank's assistance strategies during this period. Since a fairly small number were prepared and reviewed in FY88, a number of CSPs prepared in FY87 were reviewed also. They are listed in Table 1 (attached). The Reorganization Task Force report envisaged that this Review would examine questions such as the effectiveness of CSPs in providing top management with a vehicle for considering strategic and policy options, and the extent to which CSPs effectively guide Bank operations, especially lending. This report is also an input into the forthcoming FY88 Annual Review of Development Effectiveness (ARDE).

(ii) Limitations

2. This is a desk study, undertaken without discussion with borrowers or visits to the countries concerned. It is thus more limited in scope than, say, recent OED reports[1] and other evaluations in depth[2] . It was also carried out just after a new OMS was issued, very soon after the CSPs themselves were prepared, and after a period of considerable dislocation in the Bank. The findings are thus preliminary. They are based on: (a) reviews of some 22 CSPs themselves, as drafted at various stages ranging from the working level to President's Council versions; (b) comments on such CSPs by PPR, the Finance Complex, EAS and others; (c) minutes of meetings, including Postscripts to CSPs and decisions of the President; and (d) interviews with selected staff and managers from Operations and Central Departments. The views of clients on whether the Bank's strategies meet their needs are thus absent. Indeed, the whole tactical issue of whether and how the Bank's assistance strategies should be discussed with the countries concerned is worthy of study in itself.

B. NATURE OF THE CSP

(i) Its evolution

3. The predecessor of the CSP, the Country Program Paper (CPP), was introduced almost twenty years ago and quickly became a significant and successful tool of country assistance planning and program design. Its preparation absorbed substantial resources, but the Bank-wide review

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1/ Operations Evaluation Department. Sri Lanka: History of a Relationship; Pakistan: History of a Relationship; Turkey: Review of SAL's IV and V; Forthcoming reports on Tanzania and Senegal.

process becomes an important vehicle for the introduction of new operational ideas. It grew in comprehensiveness, quantification and size until 1982, after which various factors led to a reconsideration of aims and content. First, the CPP was felt to have become excessively unwieldy and costly. Second, the sharp growth of structural adjustment lending was an impetus for short strategy papers concentrating on macroeconomic or sector-wide issues. Third, the new top management of the Bank had less need for detail and apparent precision. Final, the steady growth of the borrowing country as a focus for Bank planning led in 1985 to the introduction of the Country Assistance Management (CAM) resource allocation process. The Country Program and Budget Paper (CPBP), rather than the CPP, became (and presumably remains) the tool to relate manpower and budget inputs to tasks and objectives, by country, in a detailed way.

4. The main practical use of CPPs - to develop a concensus on goals, projects, and on inputs into country programs from a variety of departments under different managements - was thus diminished. The Denning report,[3] which urged simplification of loan processing procedures and a devolution of decision-making, implied a further reduction in the need for CPP detail. In the mid-1980's various Departments experimented with short strategy papers, as the need for a revised framework became clear. New guidelines on the renamed CSPs were proposed on the basis of a task force headed by Vinod Dubey.[4] These guidelines proved to be entirely consistent with the aims of the Bank's reorganization, with its strong client orientation, and corresponding expectation of a more rigorous and carefully articulated strategy for Bank actions in and for each borrower.

5. A new OMS[5] was issued a year and a half later, but it differed in three respects from the January 1987 guidelines. First, CSPs are to have multiple audiences rather than be documents ... "exclusively designed to provide the basis for review by senior management of Bank assistance strategies...." (Stern, op. cit. para. 4). Second, the new OMS called for recommendations on Bank strategies in the major sectors and a discussion of how these relate to overall Bank strategy. Third, CSPs themselves are to include, as attachments, detailed 5-year lending programs and 3-year ESW programs, consistent with the recommended strategy, rather than limiting recommendations to ...."general orders of magnitude and broad sectoral thrust of lending and ESW.... details would be addressed each year through .... CPBP's." (Stern, Section V). These revisions, therefore, in relation to the January 1987 guidelines represented some movement back toward the more comprehensive CPP. These points on aims and content are referred to again below.

Footnote 2 Cont.

2/ e.g. From Dutch Disease to Dutch Auction .... Benjamin B. King for SPRPA.

3/ Streamlining Bank Procedures, November 4, 1985

4/ The Task Force recommendations were discussed at the OVPs meeting of 17th December, 1986, following which guidelines were on CSPs issued by Mr. Stern on January 5th, 1987.

5/ Operational Manual Statement 1.12 of July 1988.

(ii) Objectives and processes

6. The objectives of CSPs and the process of reviews are not explicitly stated in OMS 1.12. Users and reviewers perceive, however, implicit multiple objectives which lead to some difficulties which are mentioned later. First, the CSP is the main (and in countries without structural adjustment lending, like India and China, the only formal) instrument through which the Operations Committee (OC) and the President's Council (PC) can review and assess the Bank's strategy and operational programs on a country-by-country basis. Secondly, in order to provide a framework for the CPBP and thus the work program of each Country Department and the corresponding Technical Department, the CSP and the process of its preparation is intended to lead to a set of agreed goals and means at an operating level. Specific proposals for lending, ESW, technical assistance etc. can be judged against these goals in the light of available financial and staff resources. Thirdly, it provides an instrument through which operational and other staff can gain an appreciation of the Bank's global strategic agenda and the concerns of senior management, (such as the areas of "special emphasis"),[6] and apply overall Bank policies as they evolve. Fourthly, CSPs are linked to Bank-wide processes, notably, (i) the assessment of country risk, (ii) the allocation of lending resources and (iii) longer-term planning and budgeting. Usually CSPs are guided by these Bank-wide processes in the short run, but influence them in the longer run. Finally, CSP's provide a framework, so far little used, for the operations of IFC and, potentially, MIGA.

7. These objectives are in part met by the process of preparing CSPs, and in part by the documents themselves. The process of preparing and reviewing the working level draft often successfully brings together Country Department and Technical Department staffs and helps forge working level understanding both on problems to be solved and instruments to be used (Kenya, India). Reviewers from other parts of the Bank bring in experience from other countries and help develop common approaches to similar problems. As the CSP moves up the management chain it frequently undergoes changes in content and style, usually becoming more selective, and its content determine which issues will be raised at the OC level. The versions that reach top management often contain elements of advocacy or seek endorsement of strategies that in many cases are already being implemented.

(iii) Frequency and Cost

8. The total output of CSPs reaching the OC during the last two fiscal years was 22, of which only one of significance (India) was from the Asia region. Two were combined with PFPs and seven with structural or sectoral adjustment loan Initiating Memoranda. Typically, in FY87 and

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6/ Mr. Conable's memorandum of December 15, 1988 requested that all CSPs describe how the proposed Country Assistance Strategy would address the Bank's areas of special emphasis and in particular debt and adjustment, private sector development, poverty reduction, environment women in development and human resource development.

FY88, 3 1/8 years had elapsed since the previous CSP/CPP for each country. This rate of production, of eleven per year, is also that achieved during the previous two years FY85-86 for CPPs and similar documents (26), and half that intended by OMS 1.12.[7]

9. The lag appears to reflect (i) the need to give priority to lending during the disruption caused by the reorganization; (ii) the absence of firm targets for delivery of CSPs to the OC; (iii) The "echo" of earlier efforts devoted to the Baker strategy exercises in the indebted countries; and (iv) the prevalence of SALs or sector adjustment lending in the major borrowers (36 such operations in FY85-88). The fact that CSPs are relatively infrequent nevertheless makes it difficult to say that the objectives set out in para. 6 above are being achieved. In major borrowers there had been significant changes during FY86 or 87 (China, India, Brazil, Indonesia) warranting and reviewing the Bank's strategy. The absence of CSPs does not of course mean that the country managers concerned did not adjust their strategies, but the lack of the CSP instrument meant that top management was not systematically involved. Likewise, with only 11 CSPs a year, left gaps in the flow of inputs from CSP's into Bank-wide processes such as portfolio management. Perhaps in recognition of the lag in FY87 and FY88 around 40 are planned for FY89, although many are slipping.

10. While the frequency of CSP's has been less than half that intended, the average text length has been almost twice that suggested, at 26 pages rather than the 10-20 indicated in the OMS - depending on the complexity of the country. Perusal of recent CSPs suggests, though, that brevity does not well serve any of the above objectives. The topics spelt out with admirable clarity in the OMS can be covered within the suggested length only if specificity is so sharply reduced that presentations, arguments and actions are shown of subtlety and justification, indicating a need for strict prioritization.

11. The resources devoted to CSP preparation dropped from 681 staff-weeks in FY85 to 261 in FY87 but recovered last year to 501. For the past four years the average recorded cost per CSP was 25 staff-weeks, but year-to-year variations (and the comments of operational staff) suggest that the MIS data understate the cost. For example, the recorded cost in LAC of each CSP is recorded as less than half that of the other regions. If the substantial time spent by managers and reviewers is added, plus that of the reviewers in PPR, EAS, Finance, Legal, etc., it is safe to say that the cost is typically one staff-year per CSP, or about 1/2 percent of the staff input into operations in any one year. Another comparison is to say that the cost of the average CSP is equivalent to an ESW task of moderate complexity. Neither of these figures is cause for concern. Nevertheless operational staff note that adding in time devoted to sector strategies, 5-year lending programs, ESW planning, task budgeting, CPBPs, staff planning

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7/ OMS 1.12 envisages that CSP reviews would take place every two years for major borrowers (over $500 m. per year) and every three to four years for other borrowers: with 12-15 borrowers in the first category, and 50-60 in the second, this would give around 25 per year.

and periodic progress reporting in all these areas, the proportion of time spent looking inward at Bank processes, rather than outward to clients, remains too high.

C. FINDINGS ON CSP CONTENT

(i) Macroeconomic issues

12. Compared with the typical CPP in the first half of the 1980s, recent CSPs have shown a marked and increasing emphasis on macro-economic issues and, within macro issues, on the management of public sector deficits, inflation, internal debt, the balance of payments and external debt. There has been rather less emphasis on macro structural issues, such as the overall incentive framework, distributional questions, and countrywide issues affecting overall performance that may have their roots is one sector or another such as demographic change or education. Some observers note that CSP emphases are increasingly on short-run issues rather than those affecting long-run growth.

13. There are often good reasons for this shift to macroeconomics: in many countries, as the recent Report on Adjustment Lending (R 88-199, August 88) points out, fiscal discipline in many borrowers has weakened after a period of improvement. In some countries immediate and short-run liquidity crises are so severe that they dominate policy-makers' attention, and pose risks to the Bank and other lenders. There has also been a growing realization in development literature - graphically summarized in the 1988 WDR - that unsound macro policies have a significant impact on efficiency by distorting relative prices and affecting the behavior of savers, investors and producers away from that desirable for sustained long-term growth. The same point was made in the March 1988 OED review of the five Turkey SAL's. For these reasons the overwhelming emphasis on macro issues in, say, the latest Brazil CSP can be understood.

14. There is thus no doubt that the macro issues are important, particularly achieving internal balance to validate adjustments in external balance. What may be questioned, however, is whether the relative emphasis given to them is fully justified either (a) in terms of their importance in long term development or (b) their importance in guiding the Bank's operations, three-quarters of which are still investment projects rather than SAL's or SECAL's. Getting macro policies right is neither always sufficient, nor even always necessary, to produce worthwhile developmental results. There are many countries that have sustained very respectable growth rates - such as Turkey and Pakistan - despite macro policies that were far from ideal. Other countries have failed to show a supply response even after macro policies had been addressed. Questions of entrepreneurial and human development, technological and institutional change, the environment, demographic change, income distribution distortions, imperfect markets, weaknesses in the infrastructure sectors and implementation problems are all encountered as constraints on long-term change, and need to be addressed through human resource development and other social programs, and through investment lending. Addressing such subject need not

always await ideal macro policies. Furthermore, guidance is required on sectoral priorities. It is these topics that are receiving relatively modest space in most[8] recent CSPs.

15. As noted below, this stress on macro issues in CSP content is more than reinforced by the content of reviews and briefs, by the content of OC and PC discussions, and also by the choice of those to attend meetings on CSPs. Most sector and project staff in operations, interviewed during the preparation of this report, do not consider that the CSPs on their countries offer useful guidance, or that the discussions reflect a commitment to their work. This is further aggravated by the absence of a forum at the OC or PC level for the discussion of sectoral or investment issues and priorities, (see para. 31 below). The point, however, is not to emphasize sectoral and investment concerns per se, but to ensure that there is an adequate infrastructure of sector strategy analysis on which to base a judgement on macroeconomic and sectoral priorities, to integrate important themes and to select the priority issues for senior management attention.

(ii) Optimism

16. Most CSPs, like CPPs before them, and Bank documents generally, are optimistic on likely economic performance; on the likelihood that the Bank's policy advice will be taken; on the speed of introduction of policy change, and on the magnitude of results. Some observers, e.g. EAS, CEC and PPR, regard some of the behavioral assumptions, such as marginal savings rates, as "truly heroic" and often question assumptions about the availability of external capital and the response of private sector investment. There is a tendency, between one strategy document and the next or even from one draft to the next, for high case scenarios for economic performance or lending to become, for example, the base cases. This seems to be a particular characteristic of LAC CSPs. Although CSP's contain detailed projections of national accounts and balance of payments, few complement this with a quantified view of fiscal and monetary developments that would test the consistency of the external accounts. Consequently, ongoing work in PPR to develop a framework for monetary/fiscal analysis linked to income and balance of payments aggregates is of high priority. Likewise, CSPs rarely look back at the realism of the assumptions of previous strategy documents with regard to ICORs, import coefficients, tax elasticities, availability of credit to the private sector, etc. in order to temper this characteristic optimism. Recent work for the Unified Survey involving PPR and FRS as well as regional economists has improved the realism, of Country projections, but the issue remains.

8/ But not all. There are excellent exceptions such as the India CSP, and sections of the Turkey and Kenya CSPs. These, however, manage such coverage only by exceeding length guidelines. Other CSPs quite properly refer to in-depth sector knowledge and analysis but do not present it (Brazil).

17. Some degree of ambition on the part of country operational officers is both understandable, and even desirable as a way of raising one's sights. The same optimism has long been observed to exist amongst project officers[9] and the authors of the early SALs. Some countries can and will beat the averages, while others will fail. The issue is whether the optimism has gone unrecognized and leads to undue redeployment of lending and staff resources. As the Report on Adjustment Lending points out, lending is favorably regarded and rewarded by both borrowers and the Bank, so pressures to lend certainly exist. A lack of realism may thus mean the Bank has to climb down, embarrassed, from policy change expectations that were to trigger higher lending levels. So far, the optimism found in the CSPs reviewed does not seem to have gone unrecognized by commentators or led to inappropriate actions, but detection does require in depth country knowledge by reviewers, and an explicit role for them in the review process. This role is not explicit today.

18. Optimism has at least one deleterious effect, though, which is to obscure the overall problem of the inadequacy of the resources being deployed to help the heavily indebted countries. The existence of this problem is clearly identified in some PPR documents[10] in the work of the FY88 Task Force on such countries headed by Jean Baneth and in the more recent work on the Brady initiative. Individual CSPs, by their use of optimistic behavioral assumptions and corresponding lending ranges, are able to avoid addressing this overall problem - but it remains to be tackled. The Congo CSP is a typical case in point: lending would vary depending on the adoption of certain policies, but results could be jeopardized by underfunding of the external gap caused by factors beyond the control of the country or the Bank.

(iii) Trigger Points

19. All CSPs lean over backwards to avoid specifying the exact actions or achievements that would constitute adequate performance and thus trigger lending actions: operational managers prefer to keep the details for discussion in the context of a specific adjustment loan at a specific time. Regions indeed need this flexibility, firstly because there are often alternative sets of policies that can move a nation towards a particular goal, and secondly because there are tactical issues involved in deciding whether to recognize modest forward progress, or to withhold lending in the expectation of inducing more significant changes.[11]

20. There is merit, however, in ensuring that CSPs indicate at least the criteria that will be used as a starting point for assessing policy

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9/ Alfred Hirschman: "Development Projects Observed". 1967.

10/ e.g. "The Adequacy of Resource Flows to Developing Countries" DC/88-4. March 1988.

11/ There is a trade-off between candor and effective implementation of trigger points given the apparent ease with which some confidential documents can be leaked to the press and to country governments.

progress - such as quantifiable measures of more uniform effective protections, deregulation or reduction in price controls, of more efficient resource mobilization or expenditure allocation and the like. Such criteria are increasingly being specified. Being specific is a useful discipline for country economists who are thereby forced to go beyond general principles and recognize the difficulties faced by policy makers and administrators. Even though they are working in a field in which the science of measuring the net impact of a policy change - as between individuals and over time - is weak, exaggerated claims on the impact of policy change may be moderated if analysis in required to be specific.

(iv) Strategy design

21. Strategy design in recent CSPs has the particular characteristic of assuming that the Bank has the capacity to address all the problems identified in the country concerned. The question of the Bank's comparative advantage - especially in a situation in which staff resources are severely constrained - is rarely mentioned. No analysis has been seen of the basic cost-effectiveness issue, i.e., how can the Bank have the biggest developmental impact at a given resource cost. This is not easy to analyze, but in most borrowers, large or small, the Bank's constructive influence has to be earned through years of professional analysis and understanding. It is sometime tempting for the Bank to attempt to be a full-service institution, and one searches in CSPs in vain for the selectivity necessary for the development of knowledge in depth, even though the January 1987 guidelines were explicit on this.

22. One factor in deciding in what areas of the economy the Bank should seek to have a constructive impact is political. Some good political analyses are now emerging, but these tend to be at a national level, and the political factors that affect the design of, or adoption of, particular policies of concern to the Bank are weakly assessed. This is an area in which PPR could provide guidance.

23. A further characteristic of recent CSPs is that the strategic options for the country (as well as the strategic options for the Bank - not necessarily the same) seem to concentrate on those that can be measured by a range of macro-economic projections. Where the methodology is less rigorous or less developed, as in choices on, for example, the public expenditure priorities to be given to human development compared with infrastructure, or other choices that cannot be made mainly by reference to market signals (such as expenditures on preventative versus curative health care) then the topics are usually ignored. For most country program, however, the difficult choices are among sectoral priorities for which the CSP should provide authoritative guidance.

(v) Strategy Implementation and Policy Dialogue

24. CSPs are usually silent on how policy changes are to be introduced and administered by the governments concerned. Knowledge in the Bank on how policy changes are decided and implemented is weak, in marked contrast to that on how projects are designed and executed, on which the Bank is

knowledgeable, involved and accepted. The design of ESW, and the selection and retention for adequate periods of experienced staff, are critical here.

25. Nevertheless, CSPs are giving more careful treatment to the question of how to conduct a policy dialogue. Some CSPs (India) recognize that the Bank is only one of numerous forces for change (or resistance to change) and that overt, visible pressures especially in open societies may be resented and counterproductive (Brazil, Kenya). The sensitivity of the conduct of the dialogue may also result in the subject being treated orally rather than written down in CSPs (Brazil, Colombia). It is clear from the CSPs reviewed that the weight given to achieving policy change through effective preparation and dialog is rising. Some borrowers are reportedly upset at the influence claimed by the Bank; others recognize that the demonstration of influence strengthens the institution. CSPs are usually silent on the diplomacy involved - who should analyze an issue, the Bank, a local institution, or both in collaboration? with whom should discussions be held, at what level and in what sequence? Timing is all important. What is the role of the Resident Mission? Clearly CSPs cannot cover all such tactical questions, but an awareness of the limitations of the Bank's influence could help impart realism to strategies.

26. The power of the Bank to foment rethinking on policies, on the basis of first-class intellectual output, is often understated[12] It does not need to be lending-related, indeed, it is often better if it is not: continuity and trust are often essential, and discontinuity in lending in a particular sector can in some circumstances be fatal to an effective dialogue[13] as can threatening to withold lending. In other countries and circumstances, however, such a threat helps the Bank be taken seriously. In the latter case there is a merit in choosing lending instruments (usually sectoral and investment operations) that lead to a self-limiting program (as in Nigeria) if sector policy action is not adequate. This may be a better basis for a sustained dialogue than having sectoral operations hostage to macro-economic actions unless better macro policies are a precondition to satisfactory sector performance (as in Brazil). If the latter point is chosen, it is important that the CSP or underlying CEM demonstrate the link between macro policies and sectoral, or investment project, performance.

27. In the case of SECALs as well as SALs, an understanding on macro policies is essential (as emphasized in the Report on Adjustment Lending). The need for balance of payments support is justified essentially on macro grounds, and the government concerned is expected to be following policies that will reduce the need for this extraordinary form of assistance. Moreover, experience indicates that the effectiveness of policy measures supported by SECALs is strongly influenced by the adequacy of overall macro management.

12/ Benjamin B. King's recent study on the Bank's relationships with Zambia (op. cit.) affirms this point.

13/ See Pakistan (OED, op. cit.)

28. The final point on implementation is that the role of the IMF is unevenly covered. Partly this is because the IMF often participates in working-level reviews, and it is not usually desirable to use the CSP as a vehicle for a discussion of the Fund's role. Working level relations with Fund staff are often reported to be good, however, and there is constructive collaboration on the analysis of many country situations in particular. In view of the looseness of the present agreement on Bank-Fund notations, it would be desirable for CSPs to pay more attention to Bank-Fund issues.

D. COMMENTS ON CSP PREPARATION, AND CSP ROLE IN THE BANK'S PLANNING PROCESSES

(i) The Review Process

29. There is widespread appreciation by CSP authors of support from Finance, PPR, EAS and others at early stages of CSP drafting and discussion. Although receiving guidance from departmental and regional senior staff, a typical CSP author has had little experience of presenting strategic choices for the Bank (as opposed to choices for the country) and comments from reviewers are an important way of conveying cross-country information about the issues of current concern to the Bank's management and of guiding presentation and content. There is great merit in involving all review departments at the IM stage, to avoid more heated discussions later when positions have become more fixed.

30. Turning to the OC level reviews, the agendas prepared by EAS and the reviews by SPRPA and Finance have a decisive and constructive effect on the issues raised and discussed by members of the OC, and the decisions reached. There is however widespread concern in operations about the impact of the review process at the OC level on CSP content and coverage. Firstly, the composition of the OC is such that skills in, and interest in, macro-economic issues predominate, and the discussion follows suit. The brevity of the meetings means that even when (as is the case with most borrowers) there is a heavy concentration of sectoral issues and investment lending and dialog, the discussions tend to concentrate on the identified macro issues.

31. Secondly, the agenda and briefings for OC meetings and written reviews of CSPs often reinforce this tendency. No recent CSP was found on which there had been a thorough review, the outside Country Departmental by sectoral specialists, of sectoral strategies. Sectoral and project staff feel, as a result, that their contributions to the development process are not seen as part of the central work of the Bank. The concern is reinforced by the fact that investment loans are only exceptionally reviewed by the OC. Project work that is perceived as often having as high a developmental impact, including the impact of supervision, is not discussed in CSPs or in the OC.

32. Thirdly, while there was clarity on the kind of review or contribution that could be expected from the Finance complex - especially on the analysis of Bank portfolio risk, on co-financing and the use of alternative financial instruments - there was less clarity on the kind of contribution that is expected from PPR and its various components. This issue is pursued further in the recommendations section below.

33. It is not clear that the CSP review process is achieving the goal, set for it in the OMS, of ensuring that each CSP is based on assumptions about the external economic environment and country behavior that are consistent with the Bank's global projections, e.g. on capital availability and trade.

34. Finally, there are variations from Region to Region in the kind and depth of review received by draft CSPs at the RVP level. Some receive no review at all, others are reviewed but without the participation of non-regional staff.[14] In LAC, each CSP receives a comprehensive review at a Regional loan committee, providing a useful degree of cross-country fertilization. This has a visible effect on CSP quality. Unlike the role of the President's Council, which is explicit in the OMS, the role of RVPs is left open but now seems to need codification, perhaps along LAC and EMENA lines. Participation from EAS, FRS and PPR should be considered.

(ii) The CSP and the Bank's Planning Process

35. There is a lot of uncertainty over whether and to what extent the CSP is a decision tool. Some managers use the CSP to get decisions, and the minutes or Postscripts record conclusions about lending levels and composition. These decisions tend to be reflected in the Lending Allocations decided upon, even though the OMS makes it clear that final decisions on lending levels, staff resources, etc., are to be made in the context of overall Bank lending constraints and the CPBPs. Increasingly, though, lending allocations are presented as wide ranges, which leaves open the question of where and when lending volume decisions will be made. It is not clear that the CSPs can contribute suitably to final decisions on lending levels, especially if their frequency is less than a dozen a year.

36. The overall planning and budgeting process (as set out in the Reorganization Task Force's PPR report of 11 May, 1987) makes no mention of CSPs. This might suggest that CSPs are strategy documents and not the medium for bargaining over resources. To the extent that CSPs are seen as having an influence on resources, there will be a risk that CSPs will (consciously or sub-consciously) act to preserve the status quo in the allocation of staff and financial resources. This is particularly the case in the post-reorganization Bank in which, in each of the Country Departments and especially the single Country Departments, the tendency may be continue to plan for full employment of staff in each of the existing divisions, and to eschew strategies that require changes in the content of the project pipeline and large shifts in personnel. One of the merits of

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14/ The Reorganization mandated non-regional involvement at the working level review, but not at the RVP level.

the reorganization itself (as opposed to the new structure) is that it facilitated significant and hitherto unpalatable shifts in the share of resources to be devoted to work on the social sectors and poverty alleviation. The India strategy and corresponding staffing pattern is a case in point: the new strategy in embryonic form had a big influence on staffing levels, especially in human resource development.

37. CSPs are, however, crucial inputs into Bank-wide planning and resource allocation. The Lending Allocations review should verify that proposed allocations are consistent with agreed country strategies, and that specific criteria for lending allocations such as country performance, country risk, macroeconomic and sectoral priorities (all requiring articulation in the CSP) and special Bank concerns in the light of Bank priorities (as articulated in the "Framework for Strategic Choices"). Although CSPs were not intended as the medium for bargaining over resources, they would fail as strategy documents if they did not set the broad criteria and framework for resource allocation. As indicated in the earlier discussion of trigger points (para. 20), the assumptions and criteria underlying different lending scenarios should be sufficiently clear to permit verification of Country Assistance Strategy in the Lending Allocations review.

38. CSPs clearly contribute substantially to informing the Bank's judgement about country risk management and portfolio risk. Recent CSPs, helped in particular by the 1988 Country Risk Report, contain more rigorous assessments of risk and how to minimize it than in the past, and reach firm conclusions (Kenya, Brazil). Indeed this is an area in which firm decisions by the Bank are necessary, and where judgements about relative and absolute risk levels need to be made on the basis of country policy and performance expectations that are plausible, and within a framework of agreed global projections of GNP, trade, capital flows and other variables. It may not be possible to judge the framework of every individual CSP, but the set of CSPs produced in a one year period could be evaluated. This could be done in the next annual CSP review.

39. It is exceedingly difficult[15] to document what impact CSPs have had on the actions of the Bank: there are often significant differences between the lending and ESW program proposed in CSPs, and those that preceded and followed them. Indeed this is to be expected if CSPs are not the final decision tool. Usually agreed floor lending levels get incorporated into the Lending Allocations, but ceilings are diminished. Most staff find the discipline of writing a CSP useful, but recognize that flexibility is necessarily maintained because random events might intervene (Pakistan); external political pressures, e.g. by major donors are strong (Argentina); major decisions (IDA for Nigeria) are necessarily taken outside the CSP context if timing so requires; and accountability of managers for the results of their proposed strategies is modest.

15/ Not least because systematic records of planned ESW and planned lending in the two-year period before the reorganization were often destroyed in the reorganization itself.

E. CONCLUSIONS AND RECOMMENDATIONS

40. Country Strategy Papers, and especially the process which produces each CSP, clearly are valuable to the Bank. Perhaps their main achievement, like that of the CPPs before them, is to serve as a form of communication between senior managers and staff, and between different organizational units in the Bank. Like many a good management tool, CSPs also help the average manager be explicit about his goals and means, through a tool that a first-class manager would create in any case. CSPs also help develop a Bank-wide approach to tackling common problems, across countries. It is also clear that the CSPs, and the OMS that guides them, are marked improvements over the old CPPs.

41. The Review of recent CSPs leads however to some suggestions about how the tool and the process could be made more useful to the Bank. First, CSPs serve multiple audiences and objectives: the main three audiences are the Bank's top management; central staffs responsible for risk assessments, lending allocations, Bank-wide planning and budgeting, and the achievement of Bank-wide standards; and operational staff responsible for designing and deploying lending instruments. The present CSPs are uneasy compromises between the needs of these three sets of users. There is some difference, for example, between the kind of strategy document needed by operational staff as a guide to their own actions and the CPBP, and that called for in OMS 1.12 (especially if one takes literally its covering note which states "the CSP should ... focus only on the main macroeconomic and sectoral issues facing the country") which is appropriate if the main audience is top management. It should be emphasized that the primary objective of CSPs is to obtain Senior management guidance and approval of Country Assistance Strategy.

42. There is also a divergence between the needs of those who use CSPs as a basis for assessments of portfolio risk and lending allocations, for whom realism and cautious judgments about downside risks are at a premium, and those for whom both the CSP and its process are tools of advocacy and of testing whether ambitious goals are achievable. On balance, the need of the Bank is for realism, and the process that produces CSPs needs to serve that end. The review process must thus be capable of detecting over-optimism, at an early stage, and of delaying CSPs until such issues are resolved. One tool that would improve realism would be the re-introduction of unified projections of trade on a consistent Bank-wide basis for major countries, which would act as a reference point for expected performance in the balance of payments. Another tool in some cases would be the inclusion of monetary and fiscal projections linked to existing income and balance of payments projections (although perhaps a 5 year horizon for both is sufficient). Finally, extra regional staff should be more actively involved in the review process before the Operations Committee stage.

43. It seems clear that whereas the process of producing a CSP must first and foremost involve the working-level operational audience, the CPBP is the document which guides operational staff in their work. In the initial stages the CSP may contain a sizable amount of sectoral detail. As it proceeds to the RVPs and top management, however, it must be winnowed

down for this latter audience. Even here, experience to date suggests that the 10-20 page limit for CSPs is sometimes too modest for full coverage of issues in some cases, but length requirements have been dealt with flexibility. There is therefore, no need to change the OMS length guidelines at this point.

44. The OMS recognizes that different categories of countries face different problems, requiring different sets of Bank instruments, and CSPs should reflect this. One would expect quite different CSPs for:

a) indebted middle-income countries facing serious liquidity problems (Brazil, Argentina, etc.);

b) other middle-income countries (Colombia, Turkey, etc.);

c) the large low-income countries where the Bank's investments are modest relative to total investment (India, China); and

d) other low-income countries (Nepal, Tanzania, etc.).

CSP content would vary accordingly, to reflect both the problems of the countries and the strategy of the Bank, and so should the content of reviews by central departments. In view of the diversity in the CSPs that could be produced, a one or two page Task Brief should be prepared before beginning a CSP to elicit consensus on the focus of the document to be prepared.

45. For countries in all categories, however, it would be appropriate to recognize that even when there are severe macro-imbalances, development activities can and should take place in health, education, training and science, population, institutional development, technology, environmental protection, creation of opportunities for women and the like. Progress in such core fields supported when operational problems created by macroeconomic imbalances are not excessive (and where risk allows). These would stand the country in good stead when macro balances, and incentive and regulatory systems are themselves improved. As indicated earlier (para. 15) an adequate basis of sectoral analysis should exist on which to make the appropriate judgements.

46. Given the ready acceptability of advice at a working level (before departmental clearances are obtained and positions solidify), and the fact that authors do not normally have experience in Bank strategy formulation (as opposed to strategy for the country), there is a case for a central advisory role that would provide, for the two dozen teams which ought to be at work in any one year, guidance through (i) communication of best practice; (ii) digests of relevant policy work; and (iii) lessons in aid effectiveness from a variety of sources.

47. This advisory role would presumably be developed by PPR. Regarding sharing of best practice, it could be helpful to develop a series of seminars in which experienced and prospective authors of CSPs, and staff from EAS, Finance, and PPR could review experience and glean the lessons of

the CSP production and review process. These seminars could be extended by providing potential CSP authors with insights into the strategic directions and new initiatives being considered for the Bank as a whole. CSPs will need to consider outputs such as research, technical assistance, training and information services, and reflect the overall institutional goals.

48. A further support role for PPR would be to digest, for categories of countries such as the four mentioned earlier, the vast range of sector and economy-wide Bank policy work, the OED reviews of operations, and outside evaluations of aid effectiveness such as those prepared for the Development Committee as reflected in "Does Aid Work?"[16] This would provide rich lessons for the design of Bank strategies, from sources which are not normally the daily reading of CSP authors; providing access to such insights into Bank strategies would also help PPR's role become active rather than reactive. This digest role (using sources of the kind listed in Table 2) is distinct from that of disseminating economic research on country policy issues, which could help the design of national policies as opposed to the Bank's policies.[17]

49. There are useful lessons to be learned about the value of a long-term aid relationship, with continuity of staff where possible, where respect for experience and professionalism can overcome the sensitivities many from poor nations feel when confronted with a powerful establishment like the Bank. There are lessons to be learned by simply listening: project staff in Tanzania for example were aware, from field experience, that projects were failing because the magnitude of the government's reform efforts exceeded that which the administration could handle. This awareness came six or seven years before the Bank changed its lending strategy. Further themes run through success stories of aid relationships: e.g. does the activity being financed contain the seeds of increasing self-reliance? Synthesis of such points for prototypical countries would help the design of Bank strategies enormously.

50. CSPs at present tend to emphasize one kind of choice - how the Bank should respond to various levels of policy performance (emphasizing those policy changes whose impact can be captured through a quantitative model). This analysis is useful and, indeed, should be sharpened by clear discussions of the criteria by which lending would move from base to high or low case scenarios.

51. CSPs do not present or analyze other kinds of choice, however, such as how best to deploy the Bank's staff skills and lending resources so as to have the maximum developmental impact in the longer term. This is a difficult job, and requires a cool assessment of where the Bank's comparative advantage lies or could lie, and how to build on it, e.g., by ensuring there will be a critical minimum set of skills available over time to work on a particular problem, that there will be receptivity and

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16/ Robert Cassen & Associates, Oxford, 1986.

17/ A distinction not always clearly drawn in CSPs which should, to avoid confusion always be called "Bank Assistance Strategy for......".

collaboration by the borrower, and that the Bank can sustain its commitment over a considerable period. This would require some analytical work on how to quantify (as least roughly) how the country benefits from Bank involvement in a series of projects - a with/without comparison would be ideal, bringing in the concept of sustainable change. Likewise the development leverage obtained from devoting staff time to helping induce policy change (probably a high-risk, high return endeavor), or from improving procurement practices, could be assessed. Insights derived from such inquiries could help move CSPs towards an exploration of the Bank's comparative advantage, and away from their present posture of appearing to offer a Bank solution to all problems mentioned - but not mentioning these issues to which the Bank has no answer.

52. Furthermore, at present, there is less than full clarity about how to make the participation of PPR in the review process most effective. The contributions from the sector policy departments need to be strengthened; overlap between PPR and EAS, and within PPR, on macroeconomic topics could be diminished, and responsibility for assessing undue optimism pinned down. In addition, a positive guidance role of the kind outlined in the preceding paragraphs could be developed.

53. Finally, an issue remains about the ideal frequency of CSPs: 22 over FY86 & FY87 was too few for the purposes described earlier, both for the central departments and top management, and as a guideline for operating staff. The figure discussed in OMS 1.12 (25 a year) seems to be as reasonable frequency as any, and comes closer to meeting the needs of departments concerned with risk and lending allocations. This implies two CSPs a month for consideration by the OC, although there would in practice be significant bunching. A definitive list of CSPs needs to be developed between Finance, EAS and PPR at the start of each fiscal year: once the list is agreed, close follow-up and ultimately sanctions might be appropriate to emphasize the importance attached to this tool.

Summary of Major Conclusions and Recommendation

54. a) Although the CSP serves multiple audiences, its primary role is a vehicle through which to inform and elicit guidance from senior management on strategic issues. (Paras. 5, 6 and 41)

b) The CSP should focus on the most important obstacles to long term development, whether macroeconomic or sectoral. There should be an adequate basis of sectoral analysis on which to judge macroeconomic and sectoral priorities, integrate important themes and select priority issues. (para. 15)

c) CSPs should be more realistic in their assessments of likely developments (Paras. 16-18). A more formal role for extra-regional staff in Regional Vice Presidential reviews could be useful (Para 34), as could preparing projections of monetary and fiscal aggregates in many country circumstances. (Para 42)

d) CSPs should contain more explicit analysis of the Bank's comparative advantage and of political factors affecting strategy design. (paras. 21, 22, 51)

e) CSPs should contain explicit discussions of the ways that the recommended strategy will be carried out. (Para. 24)

f) Trigger points and criteria for shifting among lending levels and strategies should be discussed. (Para 19, 50)

g) Task managers should prepare a Task Brief to elicit consensus on the focus of CSPs before beginning their preparation. (Para 44)

h) PPR, with staff from EAS and experienced Regional staff, should conduct seminars to share the lesions of experience in strategy formulation with prospective CSP authors. (Para.47)

i) The number of CSPs produced annually should be maintained at around the 25 per year level called for in the OMS A definitive list of CSPs needs to be developed at the start of each fiscal year and delivery carefully monitored. (para.53)

Table 1
Basic Data on
CSPs in FY87 and FY88

Country	Operations Committee: Date	Combined with PFP	Combined with SAL/SECAL IM	OC length (pages)	Discussion at PC: Date	Years since last CSP/CPP
AFRICA						
Benin	06/22/88		No	29		3
C.A.R.	03/02/88	No	Yes	36		5
Congo	03/06/87	No	Yes	17		3
Djibouti	12/05/86	No	No	8		5½
Gabon	11/06/87	No	Yes	26	11/18/87	4
Guinea	02/03/88	No	Yes	28		3
Kenya	02/10/88	Yes	Yes	20	03/04/88	3
Nigeria	06/12/87	No	No	17	07/22/87	3
Togo	11/11/87	No	Yes	26		3½
Zimbabwe	10/20/86	No	No	28		1
ASIA						
India	06/08/88	No	No	44	07/05/88	3
Pacific Islands	10/16/86	No	No	15		5½
EMENA						
Jordan	11/10/86	No	No	27	01/29/87	3½
Pakistan	02/17/88	Yes	Yes	27	04/11/88	3½
Poland	09/22/87	No	No	21	11/25/87	n.a.
Turkey	07/25/88	No	No	37	09/31/88	1½
LAC						
Bolivia	11/25/86	No	No	31		3
Brazil	03/16/88	No	No	32	04/06/88	3
Chile	05/04/88	No	No	21	06/20/88	2
Colombia	05/27/88	No	No	37	06/20/88	1½
Guatemala	01/25/88	No	No	19	04/04/88	4
Jamaica	07/29/87	No	No	18	08/26/87	2
Totals/Ave.	22	2	7	25	12	3¼

Source: EAS

Table 2

Table 2. List of Policy Papers

The policy papers listed here - a very partial list - are typical of those which a CSP author might not have time to absorb, but which could contain ideas that would improve country strategy design.

OED
- SALs: A First Review of Experience (1986)
- Overview of Turkey SALs (April 1988)
- 1987 Annual Review of Project Performance Results (August 1988) (especially Chapter VII on SALs)
- Pakistan - A Review of a Relationship
- Sri Lanka - A Review of a Relationship
- Senegal - A Review of a Relationship (forthcoming)
- Tanzania - A Review of a Relationship (forthcoming)
- Bangladesh - Review of Experience with Import Program Credits I - X
- Rural Development 1965-86: The World Bank Experience
- Agricultural Project ERRs - a Statistical Analysis

PPR

(i) Annual Operations Reviews:
- Women in Development (FY87) (incl. review of selected economic and sector reports 1980-87)
- Population, Health and Nutrition
- Education & Training
- Agriculture
- Energy
- Transport
- Water Supply and Urban
- Industry, Trade & Finance (March 1988) [This report asks what are the binding constraints on adjustment and its speed, and also identifies the need for "cookbooks" for typical groups of countries to assist operational staff]

(ii) Other PPR reports:
- Annual Review of Bank Research (March 1988)
- Reports on Poverty Alleviation (March 1988 & August 1988)
- Strategic Agenda for the World Bank (August 1988)
- Guidelines for Bank Lending for SOEs Sector Reforms (1988)
- World Bank Operational Strategy in the Heavily Indebted Middle-Income Countries R 88-58 (March 1988)
- The Adequacy of Resource Flows to Developing Countries DC/88-44 (March 1988)
- Strategic Issues for Agricultural Lending in SSA (1988)
- Report on Adjustment Lending R88-199 (1988)
- Competition policies for Industrialising Economics (forthcoming 1988)

SVPO
- Financial Intermediation (forthcoming 1989)
- Annual Reports on Project Implementation and Supervision (1988)
- Bank's Role in Credit Enhancement and Financial Intermediation (1988)

AFRVP
- Long-Term Perspectives in SSA (forthcoming 1989)

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THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: June 22, 1989

TO: Operations Committee

FROM: Vinod Dubey, Director, EAS

EXTENSION: 78051

SUBJECT: TANZANIA: Agriculture Adjustment Program - IM

1. The Operations Committee will meet on Monday, June 26, 1989 at 3.00 p.m. in Room E-1243 to discuss the Initiating Memorandum for Tanzania: Agricultural Adjustment Program. The proposed amount is US$158.6 million, in addition to which some $150 million in cofinancing will be sought. There will be two equal tranches in early and mid 1990 and disbursements will be against a positive list (except for the technical assistance component). The presentation in the documents is excellent.

2. The various reforms to be supported by this Credit would, if fully implemented, amount to a radical transformation of Tanzanian agriculture. Output taxes, implicit in the inefficiencies of the present marketing system, would be reduced, if not eliminated, and input subsidies will also be reduced. Administration of pricing decisions would be much reduced, and the flexibility and responsiveness of the system enhanced. Changes of this type are needed and, in fact, are a sine qua non for the success of the overall adjustment program given the importance of the sector in terms of national income, employment, poverty and exports. The main issues concern the macro environment and the design of the policy changes.

Macroeconomic concerns

3. Tanzania's Economic Recovery Program has continued to enjoy the support of the Bank and the Fund, and there has been significant progress. Nonetheless serious concerns have arisen recently with exchange rate management, inflation control, and increasing arrears. While the macroeconomic performance targets will soon be renegotiated for the third-year PFP, the Region might explain the present status and the reasons why the Government finds it so difficult to stay within the agreed macro-framework. The Government's commitment to the ERP and to the radical changes being sought under the proposed Credit may also be elaborated upon.

4. The IM does not directly comment upon the inter-relations between agriculture and macroeconomic adjustments on the grounds that they are being treated elsewhere. But it may be useful if the Region comments on those linkages, in particular on the fiscal and balance-of-payments impact of the various changes being sought. Even if all the institutional and regulatory changes are implemented, it is probable that some agricultural taxes, even export taxes, will need to be introduced for revenue reasons. The Region might explain what kind of taxation in agriculture is envisaged eventually and if there are any plans to overhaul the tax system.

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SVPOP

open up the Marketing Boards - have licensed traders - How do you manage the transition

Quantitative price guidelines

Program Design

5. The IM suggests that the list given in the policy matrix can be cut down to six basic conditions (para. 70). Yet looking at the policy matrix it is not easy to see which conditionalities have been identified as being of second-order priority. The two macro-conditions would of course need to be added to this list. NMC "restructuring", seems to cover all the points under "Grain Pricing and Marketing". Similarly, the various points under coffee, cotton and cashew seem to be essential elements of the whole package of measures to be taken for each crop. The input supply conditions seem to be the only ones considered non-essential, although this does not reduce the list very much. <u>The Committee might consider this whole question of selectivity and relative priorities.</u>

Also Para not given completion of studies

6. The Committee might also consider:

- A general point is made in para 25 that "for export crops, the market-based pricing systems and the accompanying institutional changes are expected to result in producers receiving a much higher share of the export price." While true, one ought to have some notion of what the shares should be; in reforms of this type it is desirable to specify some limits beyond which domestic prices should not diverge from border prices, and to set up the technical capacity to analyze and monitor domestic-border price relationships; this may be particularly important because the administrative interventions will linger for a while, and even afterwards we need to check how efficiently the markets are working. <u>Should the covenants be therefore supplemented by quantitative pricing guidelines?</u>

Get proper relationship between domestic / border prices

- Another important general point about transition to unrestricted free markets is the question of price stability, also mentioned in para. 25. It might be useful if the Region reports on what the experience has been with respect to the stability of domestic prices relative to international prices. Furthermore, the transition to free markets may be particularly vulnerable to extreme fluctuations in international prices. <u>The Region might comment on the desirability of having a policy and some machinery to offset extreme fluctuations to safeguard the planned reforms e.g. variable export taxes for coffee and cotton.</u>

How do you prevent price instability in commodities

- Is the Strategic Grain Reserve (SGR) the most efficient way of ensuring "food security", relative to, for example, higher levels of foreign currency reserves (para. 37)? What price ceilings are considered adequate, or alternatively how are target stocks determined? What is the assurance that 100,000 - 150,000 tons would be adequate, and should there be supplementary measures?

Margin

f. exch reserves vs Strategic Grain reserves

- The Government seems to have strong reservations against private participation in cashew export. Should such participation be considered a sine qua non for this operation?

- Since fertilizers are being made available by donors at subsidized prices, the subsidized border price is the opportunity cost as long as free-market imports are not needed. It would seem therefore that the recommendation to raise fertilizer prices to the c.i.f. level (para. 59) is inappropriate at the present time.

Is the recommend re fertilizer prices right?

- In proposing basic institutional changes in the marketing infrastructure, it is important to ensure that farmers do not lose access to essential services, such as those dealing with research and extension; some marketing boards elsewhere have provided high-quality services in return for their high margins. The Region might comment on the public and parastatal sectors' contributions to essential farm services in Tanzania, and how they are to be safeguarded during the transition phase. Should some measures be explicitly introduced for this purpose, perhaps under the "Investment and Recurrent Budget category"?

- Attention is also required to the disbursement provision for the operation: all commodities included under OGL would be eligible for financing whether pertaining to the agriculture sector or not. Is disbursing against a general positive list appropriate in this case?

General positive list?

Operations Committee

Messrs. Qureshi, Husain, Jaycox, Karaosmanoglu, Thalwitz, Rajagopalan Fischer, Shihata, Wood, Vergin

cc: Messrs. Lee, Shakow, Holsen, Rao, Burmester/Thahane. Liebenthal, Steer, Baudon, Hopper, Bock, Goldberg, Kavalsky, Parmar Pfeffermann, Baneth, Robless, Ms. Haug, Tanaka, Agarwala Sandstrom, Messenger, Ali, Olivares

ARay:gs

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

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OFFICE MEMORANDUM

DATE: June 14, 1989

TO: Mr. Moeen A. Qureshi, OPNSV

FROM: Michael J. Gillette, Acting Vice President, AFR

EXTENSION: 34000

SUBJECT: TANZANIA: Agricultural Adjustment Program Initiating Memorandum

1. The attached Initiating Memorandum seeks authorization to appraise in June 1989 a proposed Tanzania Agricultural Adjustment Program (TANAA), aiming at Board presentation in December 1989. The proposed program would be supported by an IDA credit of US$158.6 million and estimated cofinancing of US$150.0 million.

Background

2. Tanzania is emerging from a long period of economic decline that began in the late seventies. Besides external elements, the most important factors were the weaknesses in macro-economic management including inadequate incentives and investment in agriculture, over emphasis on industrialization, excessive administrative controls over the economy, and overly rapid expansion of the public sector. Between 1978 and 1982, GDP only grew by 0.4% per annum, inflation accelerated to about 30% and fiscal deficits averaged about 16% of GDP. Agriculture was particularly hard hit, due largely to low producer prices and massive inefficiencies in state-run marketing boards. Production of food crops failed to keep pace with population growth and the value of exports dropped from US$426 million in 1978 to US$286 million in 1985. The decline in exports contributed significantly to Tanzania's growing balance of payment gap and marketing board losses of up to 8% of GDP have led to an excessive expansion of credit and high inflation rates.

The Adjustment Program

3. Government in 1986 launched the Economic Recovery Program (ERP), including macroeconomic and trade liberalization measures in support of restored economic growth and monetary and fiscal stability. IDA has provided assistance to ERP through the Multi-sector Rehabilitation Credit (MRC), to be closed at the end of June 1989, and the Industrial Rehabilitation and Trade Adjustment Credit (IRTAC) and the IMF has provided support through a standby arrangement and a Structural Adjustment Facility (SAF). A first-year Policy Framework Paper was agreed in October 1987, followed by a second-year PFP in November 1988.

4. There has been encouraging progress in implementation of the ERP, as exemplified through the operation of IRTAC. Significant progress has been made in trade policy reform, foreign exchange allocation, tariff and sales tax reform, export incentives, internal pricing deregulation, and deconfinement. Specific measures have included exchange rate

devaluation of over 700 percent since early 1986, maintenance of fiscal discipline, elimination of price controls on over 400 commodities, and progressive liberalization of the trade regime through the introduction of the Open General License facility (OGL). Sectoral reform measures have also been introduced in industry and agriculture (higher producer prices for export crops and initial steps to liberalize maize marketing and improve input distribution). The response to ERP has been encouraging. GDP growth of 3.4% in 1986 exceeded population growth for the first time since 1980 and the rate is estimated to have accelerated to 4.0% in 1987 and 1988.

5. There are, however, areas where some shortcomings have emerged. In particular: (i) export performance seems to be lagging behind expectations because of poorer than expected export performance in agriculture and non-traditional goods; (ii) reserves continue to decline while arrears increase; (iii) credit expansion has been higher than anticipated (net domestic assets in the banking system have increases substantially above the SAF ceilings, due in part to continued losses by crop marketing boards); (iv) inflation rate is still relatively high (25-28%), and (v) the parallel exchange rate has gone up by almost 50% over the last six months, much faster than the official rate. One particular area of concern is the exchange rate movement, which since the beginning of 1989 has not fully compensated for structural changes and relative price movements. Important economic distortions remain, requiring determined policy and institutional reforms. The proposed operation is designed to deal with critical shortcomings in trade policy and agricultural marketing that have contributed to the overall poor performance in the macro economy. In particular, agricultural exports and credit expansion are the specific areas which should respond to the measures to be adopted under this operation.

6. The Bank and the IMF are in substantial agreement in their analysis of the shortcomings in the existing program, and are working in close cooperation in getting Government to address the issues more effectively. A Fund mission has recently returned from Tanzania and discussions are continuing this week with Government officials in Washington, though no early agreement is expected. Nevertheless, the maintenance of an appropriate macroeconomic framework, through continued adjustment of the exchange rate and discipline in implementation of fiscal and monetary policies, is of particular importance for the success of the proposed operation. These macroeconomic issues will be addressed in the upcoming PFP negotiations, and agreement with Government will be a condition for Board presentation.

7. The Government has been implementing ERP in face of difficult constraints imposed by Tanzania's political legacy and the painstaking process of consensus building required both within the ruling party and among Government policy makers. Occasional delays in the program are inevitable while internal support for change is garnered. Nevertheless, as long as the consensus for change can be sustained and strengthened, continued success can be expected in implementation of the program.

The Proposed Operation

8. For the long-term, we envisage an agricultural economy largely dominated by market forces, with the private sector, including cooperatives, assuming prime responsibility for marketing all domestic food and export crops. The role of Government would be limited to the provision of basic market services and essential regulatory functions.

9. To further this long-term objective, TANAA would support radical policy and institutional changes that would fundamentally transform the current pricing and marketing systems for food crops, the major export crops and farm inputs. Key changes would include: removal of the remaining restrictions on maize and rice marketing; phasing out of direct Government involvement in the marketing and pricing of coffee, cotton and cashewnuts; restructuring of the respective marketing boards in accordance with their reduced roles; and the development of multi-channel systems for the distribution of farm inputs. The changes in pricing policy and marketing structures are expected to enhance producer incentives, improve marketing efficiency, and increase the quantity and quality of agricultural exports. Rough estimates of the income transfers to farmers from the increased efficiency in pricing and marketing for cashewnut and coffee alone are in the range of US $20.0 million per year. TANAA would also help maintain key fiscal and monetary balances through reduced marketing losses and improved efficiency in public investment in agriculture.

10. Detailed conditionality for this operation will be defined at appraisal. At this stage, a rather long list of possible conditions has been identified (see policy matrix at Annex 2). Those that are considered key elements in the policy package TANAA would support, are listed in paragraph 70 of the attached Memorandum.

11. Overall, TANAA would be an important component of Tanzania's macroeconomic adjustment and medium-term strategy. The inter-relations between agriculture development and macroeconomic adjustment are dealt with in detail in the draft Country Strategy Paper which we are circulating simultaneously to the Operations Committee. These inter-relations are not, therefore, analyzed in detail here. The policy changes to be introduced under TANAA are supported by the IMF and the major donors, and closely linked to the actions and investments they are supporting. The changes are also complementary to the adjustments pursued under the two previous adjustment operations (MRC and IRTAC, both of which show a good implementation record) and the proposed FY91 Industry and Finance Restructuring. Moreover, they complement the investment projects currently under implementation or proposed in the agricultural sector. These include the Agricultural Export, Research, and Extension projects currently being implemented, the proposed Cashewnut and Coconut Tree Crops and Agricultural Credit projects, as well as complementary projects in the transport sector (Roads, Ports and Railways).

12. TANAA would significantly contribute to achievements in areas linked to the Bank's major African initiatives. It would help improve food security at the national and regional levels, through better supplies and lower prices for the consumers of food staples. It would facilitate, and make more effective, the introduction of improved extension methods and would have no significant negative impact on the environment. Regarding the social dimensions of adjustment, the project's impact would be beneficial for most of the poorest segments of the population, although farmers in remote areas may see an initial income reduction due to elimination of panterritorial pricing.

13. TANAA is one in a series of operations to support structural adjustment in Tanzania under the ERP. Taken together, the operations support progressive structural reform in the economy at large through proper management of the key macroeconomic variables, while at the same time addressing policy and institutional changes in a particular sector. The proposed Credit would provide quick-disbursing foreign exchange resources to support the country's balance of payments and would be disbursed through the expanded positive list of the OGL.

Status of the Policy Dialogue

14. The Bank in close cooperation with the IMF, has been conducting an active policy dialogue with the Tanzanian authorities, and most of the issues addressed in the attached Initiating Memorandum have been discussed with them. For the proposed TANAA operation, we do not anticipate disagreement on the direction and content of the policy changes to be supported. Actually some of the policy reforms to be supported under the Credit have been already adopted (particularly on maize marketing), and there is agreement on implementation of others. But the timing and pace of implementation of the remaining measures require further discussion at appraisal. Some of the proposed policy or institutional changes are controversial, particularly the participation of private traders in export crop marketing, and are likely to face opposition from some quarters in the Government and the Party. Nevertheless, we are satisfied that the substantial areas of agreement identified during the extended policy discussions with Government and the supporting preparation work provide sufficient grounds for appraisal.

Attachment

DISTRIBUTION:

Operations Committee Members	Messrs. Karaosmanoglu (ASIVP); Thalwitz (EMNVP); Husain (LACVP); Wood (FPRVP); Shihata (LEGVP); Rajagopalan (PREVP); Fisher (DECVP); Vergin (OPNSV)
Other Attendance	Messrs. Lee (CODDR); Dubey (EASDR) (2); Shakow (SPRDR) (2); Holsen (CECDR) (3); Rao (FRSDR) (2); Burmester/ Thahane (SEC); Liebenthal (SPRPA); Steer (FRS); Baudon (OPNSV)

For information:

Outside Region	Messrs./Mesdames: Hopper (SVPPR); Stern (SVPFI); Bock (DFSDR); Goldberg (LEGOP); Kavalsky (FRM); Parmar (CIOVP); Pfefferman (CEI); Baneth (IECDR); Robless (OPNSV); Haug, Tanaka (EXC); Frank (CFPVP); El-Rifai (MIGPA); Rajapatirana (EAS); Obidegwu (SPRPA); Serven (CECMG); Petit (AGRDR); Knudsen (AGRAP); Adu (LEGAF); Renkewitz (LOAAF); Lister (ASIAG); Mates (LATIE); Mwachofi (CA2D1); Ramadan (CPOSO)
Within the Region	Messrs./Mesdames: Denning, Birnbaum, Ohri, Reutlinger (AFRVP); O'Brien, Armstrong, Noman (AFRCE); Wyss (AFTDR); Agarwala (AFTSE); Peberdy, Thillairajah (AFTAG); Christoffersen (AFTEN); Hindle (AFTFS); Ferroni, Cotlear, M. Ali (AF1SD); Sandstrom, Singh (AF6DR); De Ferranti, (AF6PH) (2); Cook (AF6IE) (2); Sam (AF6IN) (2); Ali, (AF6AG) (10); Messenger, Grawe (AF6CO) (6); Porter, (AF6TA) (2)
	Information Center
IMF	Messrs. Bonangelino; J. Simpson

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THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE: June 20, 1989

SAL

TO: Operations Committee

FROM: Vinod Dubey, Director, EAS

EXTENSION: 78051

SUBJECT: NIGER - Education Sector Adjustment/Investment Project (Hybrid); Initiating Memorandum Agenda

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1. The Operations Committee will meet on **Monday, June 26, 1989, at 12:00 noon in Room E1243** to consider the Niger Education Sector Adjustment/Investment Project (Hybrid) Initiating Memorandum. The following represents a proposed agenda for the meeting.

Background

2. One of the poorest countries in Africa with very limited natural resources, Niger, has one of the lowest adult literacy rate in the world (14% of the population). The school enrollment ratios for primary, secondary and higher education are well below the regional averages in Africa.

3. The macro-economic program for 1989-91 is defined by the Policy Framework Program, which focuses on structural reforms, among others, on public resource management. According to the Region's transmittal memorandum, on balance, the program is on track. The Committee may want to be briefed by the Region on the state of the macro-economic adjustment program and to gauge the level of country commitment to the adjustment programs that are ongoing.

Justification for the Hybrid Format

4. The proposed investment project involves a total financing cost of US $55 million including a quick disbursing element of $20 million. The IDA financing of this project is proposed to be $20 million, with five other donors taking up the rest. The Committee may want to ask the Region to explain their reason for the choice of a hybrid format in this operation and to elaborate on the linkage of the project to the macro-economic and sector adjustment program?

Disbursement Procedure

5. The quick disbursing component is proposed to be made against general imports, with a negative list, in three tranches of equal size. Conditionalities for these tranches are listed in Annex 2 and link the actions to the investment program in the sector. The Committee may want to ask the Region why disbursement against a positive list is not the chosen vehicle?

Are they too ambitious

Sector Issues

6. The proposed operation continues IDA's support of the reforms and improvements in the educational sector. The policy reforms contained in the Initiating Memorandum are already embodied in a Letter of Development Policy to the Government. The Committee may want to ask the Region about the state of the sector dialogue with respect to the structural reform of the education and human resources sector. What is the level of Government commitment to the specific reforms being planned, especially since some of the reforms are politically sensitive at least in neighboring countries?

7. The Initiating Memorandum describes quite clearly the objectives and scope of the project. It covers broad measures designed to improve the efficiency and effectiveness of resource use in the education sector; improvement of primary education; and the functioning of the labor market. This implies many intervention points in the human resources sector and gives the impression of a complex investment operation involving many components. The Committee may want to ask the Region to explain whether the complexity of the investment objectives could be addressed by this proposed operation. Should a larger commitment of resources to this sector be required to achieve all the proposed objectives? Are there some aspects of the proposed operation which are less crucial at the moment which could be addressed more fully in subsequent operations?

cc: Messrs. Qureshi, Shihata, Rajagopalan, Fischer, Wood, Jaycox, Karaosmanoglu, Thalwitz, Husain, Vergin, Gillette, Lee, Shakow, Holsen, Rao, Burmester/Thahane, Agueh, Steer, Baudon, Fredriksen

For Information Only

cc: Messrs./Mmes Hopper, Frank, Parmar, Goldberg, Bock, Pfeffermann, Baneth, Kavalsky, Haug, Tanaka, Robless/Lawrence, Agarwala

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THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

890612013 1.

DATE: June 12, 1989

TO: Mr. Moeen Qureshi, Senior Vice President, Operations

FROM: Michael J. Gillette, Acting Vice President, Africa Region

EXTENSION: 35040

(23)

SUBJECT: NIGER -- Proposed Education Sector Adjustment/Investment Project (Hybrid) Initiating Memorandum

1. Through the attached Initiating Memorandum we seek your approval to appraise the above project, which is a hybrid operation consisting of an integrated package of key sectoral policy reforms and physical investments. The appraisal mission would depart end June 1989.

2. Background. Niger is among the five countries in the world that have both the lowest level of adult literacy and the least developed primary education. The hybrid format was chosen because to effectively address this issue will require both major changes in existing policies, including politically sensitive reforms, as well as investments to support these reforms and ensure an adequate level of resources in this key social sector during the current period of economic adjustment.

3. Policy reforms. The policy reforms described in this IM are contained in a draft Letter of Development Policy which has been approved by the Government and is expected to be transmitted to IDA shortly. The reforms would: (a) promote more efficient and effective use of existing resources in the education sector (through more intensive use of teachers in primary and secondary education, consolidation of programs in teacher training colleges and higher education to avoid duplication, containment of student subsidies and administrative costs, and promotion of private financing of education); (b) accelerate the development of primary education (through increasing the share of the education budget devoted to this level of education and to training materials, and promotion of female enrollment); and (c) improve the functioning of the labor market for trained labor (through abolishment of pre-recruitment to the civil service, and reduced market rigidities). This reform package would reinforce key elements of Niger's overall adjustment program, particularly as regards the promotion of more efficient public resource management (para. 6).

4. Investments. The investment component would focus on, inter alia: ensuring the availability of education materials and needed school construction in primary education; restructuring and consolidating teacher training colleges and vocational training centers; developing functional literacy programs; reorienting higher education to better reflect trends in labor market demand; and strengthening the planning and managerial capacities of the education sector.

5. Project costs and financing. Total project cost is estimated at US$55 million, of which $US20 million quick-disbursing. It is proposed that IDA's share of project financing be US$20 million. The distribution of this amount between the adjustment and investment components will be determined in light of the amount of cofinancing available for each component. Five other donors have expressed firm interest in cofinancing the project -- Canada, France (FAC), FED, Germany (KFW) and Norway. A major part of this cofinancing would be within the framework of the SPA.

6. Macroeconomic framework. In 1986, Niger launched a structural adjustment program aimed at increasing the efficiency of resource use and strengthening the country's resource base, as well as improving the balance of payments and public finance position. The program has been supported by IDA through SAL I, which has focused on public sector management, the parastatal sector and agricultural policy, and the Public Enterprise Sector Adjustment Program (PESAP), which supports additional policy reforms in the parastatal sector and in public resource management. In close cooperation with IMF and Bank staff, the Government has prepared a medium-term Policy Framework Paper (PFP) for 1989-91 that focuses on broadening the scope of structural reforms in the areas of public resource management, private sector development and agricultural policy. The PFP includes a medium-term financing plan which is consistent with the macroeconomic framework and available financial resources. On balance, the Government's adjustment program is on track, and a Bank mission is presently in the field to review progress towards satisfying the conditions for Third Tranche release under the PESAP. Preparation of a proposed second SAL will be initiated by the same mission.

7. Key issues to be addressed during appraisal. The investments to be supported under the proposed project are in an advanced state of preparation, and there are no major issues. Most of the reform measures included in the policy package had been discussed within the Nigerien administration over the last several years but had, for various reasons, not been finalized. Thus, most of these reforms address concerns that were originally identified by Nigerien authorities, have matured over several years and are, in a real sense, owned by the Government. Nevertheless, despite the Government's commitment, there is always a risk that it will find it difficult to implement the more politically sensitive elements of the policy package: e.g., limitations of scholarships, abolition of pre-recruitment to the civil service, more intensive use of teachers, and reduced rigidities on the market for trained labor. The appraisal mission will pay particular attention to these issues.

Attachment

cc: Members of the Operations Committee: Messrs. Qureshi (2), Vergin (OPNSV); Jaycox (AFRVP); Husain (LACVP); Karaosmanoglu (ASIVP); Thalwitz (EMNVP); Rajagopalan (PREVP); Shihata (LEGVP); Wood (FPRVP); Fischer (DECVP)

cc: Messrs./Mmes Lee, Ettinger (CODDR); Dubey (2), Sicat (EAS); Hopper (PPRSV); Stern (FINSV); Shakow (SPRDR); Liebenthal (SPRPA); Holsen (CECDR); Rao, Steer (FRS); Baneth (IECDR); Kavalsky (FRM); Baudon, Robless (OPNSV); Bock (DFS); Haug, Tanaka (EXC); Goldberg (LEGOP); Haddad, Verspoor, Wilson (PHREE); Hamilton (PHRDR); Ohri, Denning, Edstrom (AFRVP); O'Brien, Swamy (AFRCE); Gillette, van Beuzekom, Laporte (AF5DR); Christoffersen (AFTEN); Agarwala (AFTSE); Wyss (AFTDR); Parmar (CIOVP); Frank (CFPVP); Pfeffermann (CEIED); Lietard (CA1D1); Sacerdoti (IMF); Hinkle, Key, Clement-Jones, van Eeghen, Photos (AF5CO); Socknat, Zymelman, Salomé, Moock (AFTED); van Beek (LEGAF); Weindler (LOAAF); Agueh, Fredriksen, Brown, Mazza (AF5PH); Bauer (AF5IE); Steeds (AF5AG); Watson (AF5IN); Sanger (Res.Rep.)

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June 23, 1989

CONFIDENTIAL

Minutes of the Operations Committee meeting to consider SAO TOME AND PRINCIPE: Second Structural Adjustment Credit held on June 23, 1989 at Noon in Room E-1243

A. Present

Committee	Others
Messrs. M.A. Qureshi (Chairman)	Messrs. J. Adams (AF4CO)
E. Jaycox (AFRVP)	Ms. M. Azevedo (AF4CO)
H. Vergin (OPNSV)	T. Baudon (OPNSV)
D. Goldberg (VPLEG)	F. Chaudhri (EAS)
S. Asanuma (AS1DR)	P. Crevier (SECGE)
J. Holsen (CEC)	F. Earwaker (SPRPA)
E. Wessels (LATDR)	V. Fretes-Cibils (AF4CO)
J. Linn (DECVP)	C. Koch-Weser (AF4DR)
	C. Morin (LEGAF)
	A. Noman (AFRCE)
	Ms. J. O'Connor (AF4CO)
	Ms. V. Rosenthal (AF4CO)
	Ms. J. Salop (AF4CO)
	K. Siraj (CODOP)
	T. Gibson (IMF)

The meeting was called to consider the Initiating Memorandum (IM) for the Second Structural Adjustment Credit. The amount proposed is $9.5 million, to be disbursed in three tranches. The discussion followed the agenda issued by the EAS on June 22, 1989.

B. Discussion

At the Chairman's invitation Regional representatives described the country situation. They stated that the country's institutional capacity is extremely limited, while transforming the economy from a centrally planned to a market-oriented system is complex and difficult. The debt overhang is a serious constraint on progress, and the private sector is small and weak. The Region acknowledged that the first SAC was over-designed and has recommended that the second needs to selectively concentrate on measures to stimulate a strong supply response. Since the IMF has the lead on macroeconomic management issues, the proposed operation will focus on a few structural issues, especially those dealing with the public investment program (PIP) and external debt problems. The Committee was further informed that the forthcoming CEM will address the longer-term issues and that a CSP will be prepared in the next fiscal year.

On the Chairman's query, the Region confirmed that the macroeconomic conditionality for SAC II was essentially the same as that of the IMF program.

One committee member observed the enormous imbalance between the proportions of investment in the public and private sectors (96% vs 4%) and asked whether the policy postures especially in the cocoa sector were the right ones. The Region's response was that adequate adjustment will take considerable time, and that the search for alternatives to cocoa is being intensified. The yield level in cocoa also continues to be well below the achievable potential.

The Chairman and another committee member asked whether the Social Infrastructure Fund (SIF) will really help the small entrepreneurs, whose needs require different skills than those engaged in developing infrastructure? The Region responded that the SIF consisted of three components: economic infrastructure; social infrastructure and private sector development. The Region will monitor progress in these areas, and will closely assess the proposed private sector interventions. It is anticipated that SIF will primarily concentrate on infrastructure development.

Turning to the country's public sector investment (PIP), the Region informed the Committee that, as part of the PFP discussion, the staff had discussed the PIP with the Government in February 1989 and now during appraisal it proposes to assess progress of the PIP implementation. As to the question whether there was adequate indigenous capacity to review PIPs, the Region responded that it was not yet there and it clearly needed priority attention.

The Chairman raised questions with respect to inflation, demand management and growth prospects. The Regional and IMF staff responded that, despite weak statistics, demand management and growth promoting policies were in place, inflation had recently decelerated and, overall, the country had achieved good progress in stabilizing the economy. Now the supportive measures to stimulate a supply response are needed.

On conditionality, the Chairman observed that greater specificity was needed in land distribution and other proposed actions.

Another committee member pointed out that Bank disbursements next year will be equivalent to 50% of the country's GDP. In his judgement, in the future, greater emphasis was called for on investment projects rather than adjustment lending. It was pointed out the country depended heavily on foreign aid and needed debt reduction measures. The Region noted that as a small country the Bank's points of intervention were limited. This explained our efforts and multi-sector operation and the broad range of activities included in each project. The region also informed the OC that a considerable amount of work and effort have gone into analyzing the debt issues - including debts owed to the USSR - and feasible approaches were reviewed during the Round Table in March and are being followed up at present.

Conclusion

The Region was authorized to appraise the proposed second SAC, taking into account the above-mentioned observations and recommendations.

July 03, 1989
FMChaudhri:gs

THE WORLD BANK
Operations Committee

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Minutes of the Operations Committee to Consider
ZAIRE - Social Sectors Adjustment Project
Initiating Memorandum

Held on Friday, June 23, 1989, in Room E1243

A. Present

Committee		Others	
Messrs./Mmes	M. A. Qureshi, Chairman E. V. K. Jaycox, AFRVP W. P. Thalwitz, EMNVP H. N. Scott, LEG F. X. Colaco, PREVP J. P. Einhorn, FPR S. Asanuma, ASI E. Wessels, LAC H. Vergin, OPNSV	Messrs./Mmes	P. Isenman, AF3DR V. Dubey, EAS A. Colliou, AF3PH J.-L. Sarbib, AF3DR J. de Leede, AF3CO E. Scanteie, AF3CO T. M. Jones, LEGAF G. P. Sicat, EAS J. F. Baudouy, AF3PH S. J. Ettinger, CODOP M. Guerard, AFRCE C. F. Obidegwu, SPRPA T. Baudon, OPNSV

B. Issues

1. The Operations Committee followed the agenda prepared by EAS. The main issues were: (a) the relationship of the social sector operation to macro-economic adjustment, including the conditions relevant to the investment side of the project and the need for guidelines related to hybrid operations; and (b) sector issues, including the implementation mechanisms through NGOs and the role of the Government in the sector.

Link of the Social Sector Issues with Macro-economic Adjustment

2. The Region noted that the proposed operation was similar to the Energy Sector Credit, which tried to introduce sector reforms and link these to macro-economic performance. In this regard, the Fund and the Bank are undertaking monthly reviews of the macro-economic situation to be sure it is on track.

3. The Chairman observed that the linkage of the macro-economic program stated in Annex 4 of the Initiating Memorandum should reflect more clearly the meaning of "satisfactory macro-economic" performance. A member stated that conditionalities related to tranche release should refer to specific macro-economic conditions, when there is no SAL in effect. However, if a SAL is currently in place, the reference to

macro-economic performance should refer to performance under the SAL. The Region explained that with the second tranche of the SAL already released, it would be more appropriate to refer to the PFP. The Chairman agreed that there should be both general and specific macro-conditions, but that the general conditions should be expressed in a clear, monitorable manner.

4. Macro-economic Conditions and the Core Sector Investment Projects: Need for Guidelines. The Region said that it realized that, in the case of a policy-based sector loan with investment components, unsatisfactory macro-economic performance would affect part of the investment program. When the quick-disbursing element is not released because of unsatisfactory macro-economic performance, some sector investment expenditures would be abandoned. But there is a core program that would be adjustment-proof and that should be pursued even when the macro-economic performance is inadequate. The task would be to identify those investment programs and projects. The Chairman stated that there is a need to develop guidelines that spell out the situations that are triggered by the release of the quick-disbursing elements in hybrid operations.

5. Another member focused on the issue of what determines the non-project component of the hybrid, which depended essentially on a balance-of-payments justification and also on budgetary needs. In the case of the social sectors, it could be argued that the domestic budget is unable to support essential public expenditures during adjustment, so there is a budgetary justification. But he found it difficult to find a balance-of-payments link.

6. The Region stated that the adjustment program under the PFP is utilized to influence the social sectors within a country to provide the necessary core commitments to undertake reforms. These sectors turn out to have the weakest ministries and require support because of their importance to development.

7. As regards the balance of payments, the Region noted that the SAL had been in effect for two years, suffering a delay when it went off track. It was never intended to cover the balance-of-payments needs for FY 90 and beyond. There was a new balance-of-payments need as the country's program was restored, and this requirement for quick-disbursing assistance is being financed in the context of burden sharing through SPA and the Fund/Bank PFP framework. The quick-disbursing portion of the SSAC, like that of the Energy Sector Credit, is an important element of the Bank's contribution to meeting this balance-of-payments need.

Social Sector Issues

8. Responding to the Chairman's query regarding the groups that the proposed sector program is trying to reach, the Region said that the project is designed to focus on viable social service delivery programs directed to poor regions. The project was designed to give renewed emphasis within the public expenditure program to the social sectors, specifically health, population and education. For instance, interventions in the preschool areas involved a package consisting of immunization, malaria control and family planning.

9. Targetting by type of program would reduce user charges for the poor without sharp reductions in overall cost recovery and without administratively infeasible efforts to target by income level of recipients. The project would also involve the use of NGOs, which are already operating extensively within the country. The project involves a definition of the role of the government and NGOs to assure that specific roles are recognized and supported by an appropriate funding mechanism.

10. Some members questioned the proposed NGO fund, especially government funding for it and the fund allocation mechanism. One member suggested the need for a strong audit covenant attached to the project. Another member said that the government could exercise unduly strong control on a program supposed to be implemented by NGOs by funding only those it favors. Some mechanism was therefore required to provide some objectivity in the fund allocation mechanism. The Region stated that this concern was addressed in the project's design by the creation of a national NGO board to provide representation of large and small NGOs. This board could help to protect the small NGOs from being eliminated in the funding allocation. The proposed NGO fund would represent only a small part of the SSAC and would serve as a pilot activity. The Region further stated that the Government, in the past, had been systematically withdrawing from social service delivery in favor of NGOs, and that the problem now is partly to delineate the specific role that the Government must play. It must not retreat altogether from its responsibilities for education and health.

11. One member noted that the project represented an interesting mix of poverty concerns, women in development and family planning in the social services. However, he expressed concern that the program would be difficult to implement, since it involved new institutional mechanisms and framework. The Region noted that the project would rely mostly on existing institutions and programs, that help in supervision would be provided by UNDP financing and from the SDA project, and that there would be elements in the project and in the related education project to improve the implementation and monitoring capability of the ministries concerned.

12. Another member suggested that the Zaire project would provide a good example for IDA to monitor social sector expenditures. An effort should therefore be undertaken to address per capita social sector spending and to provide some mechanism for monitoring these expenditures going forward.

Decision

13. The Chairman stated that the proposed operation represented a good project. The Initiating Memorandum was approved, and the Region was given the authority to appraise.

14. The Chairman asked the Region go over Annex 4 more carefully and to pick only those conditions that were essential for tranche release, while keeping track of other performance criteria for overall guidance.

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June 29, 1989

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THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

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Many agencies involved

DATE: June 20, 1989

TO: Operations Committee

FROM: ~~Vinod Dubey~~, Director, EAS VDubey

Not have an adequate import content in sector policies

EXTENSION: 78051

SUBJECT: ZAIRE - Social Sector Adjustment Credit Project; Initiating Memorandum; Agenda

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1. The Operations Committee will meet on **Friday, June 23, 1989, at 5:30 p. m. in Room E1243** to discuss the Initiating Memorandum for Zaire Social Sector Adjustment Credit Project. The following is suggested as an agenda for the meeting.

Background

2. Zaire's economic adjustment program was recently put back on track with the release of the second tranche of the SAL and the renegotiation of the second-year PFP. The Operations Committee in its meeting of May 26, 1989, approved the Initiating Memorandum for a proposed Energy Sector Credit which includes a quick disbursing Credit of US $90 million. At that meeting, a full review of the macro-economic and other recent developments in Zaire were discussed.

Energy sector policies allow for policies

Macro-economic Policy Linkage

many components

3. The proposed operation addresses the social sector adjustment issues in Zaire and contains a provision for a quick disbursing component of US $60 million to be disbursed in three tranches. The Region justifies the quick disbursing element as a supplement to SAL I, in that it is linked to satisfactory completion of macro-conditionality with respect to the agreed public expenditure, especially the foreign expenditure of the Government. On this basis, the Region proposes that the disbursement of this quickly disbursing component be against general imports subject to a negative list. The Committee may ask the Region to explain the reasons for assuming that the SAL requirements are underfunded and why no additional macro-economic conditionality is required. Are not the sector policy changes adequate to justify the quick disbursing element as a link to the macro-economic adjustment? The Committee may further ask the Region to discuss the prospects for greater burden sharing of assistance in the case of Zaire. Are there new developments along this line now that the adjustment program is back on track?

Macro economy

Social Sector Issues

4. The Region wants to undertake interventions in the social sector through this proposed operation through: (a) adequate reorientation of public expenditure in the social sectors; (b) promotion of increased private sector participation in the delivery of social services; and (c) introduction of new sectoral policies in education, health, nutrition and population.

5. The Committee may ask the Region to provide a tour d'horizon of the social sector situation in Zaire during the recent period of macro-economic difficulty and to relate this situation to that prevailing in similarly situated countries in Africa, taking into account employment, wage trends and the incidence of poverty. The Region may further elaborate on the prospects of alleviating poverty given the current budgetary realities in the country.

6. Protecting the Poor Through the Budget Allocation Process. The Committee may want to ask the Region to clarify the steps being proposed to protect the social service delivery system under the budgetary process. How is the targetting of social expenditures to be achieved for the poor especially in this proposed operation?

7. Promotion of Private Sector Delivery of Social Services. The Committee may want to ask the Region how the proposed operation hopes to encourage and institutionalize the delivery of public social services through the private sector and through local governments. What are the cost implications of this method of delivery compared to one in which the Government sector undertakes the same? Would the NGOs that are proposed to help implement the program be fully dependent on Government support? What criteria are proposed to be used in choosing the NGOs that would participate in program delivery? How sustainable is this method of service delivery, given that it is financed by budgetary transfers from the central Government?

8. Social Policies in the Sectors. The Region may be asked to elaborate on the new or additional policies in the social sector with respect to health, education, family planning and employment that are proposed to be accomplished under the proposed Credit. What methods of follow through are being designed that would enable the appropriate monitoring of the effectiveness of these policy changes?

Project Design

9. The project requires several implementing agencies and assumes a substantial amount of coordinative administrative capacity to implement the program. Given the limited administrative capacity of the country, the Committee may wish to ask the Region whether this complex design is not likely to reduce its implementability. What steps are planned to raise the implementing capacity of the Government in the social sectors, and in general, to assure the sustainability of the social programs?

cc: Messrs. Qureshi, Shihata, Rajagopalan, Fischer, Wood, Jaycox, Karaosmanoglu, Thalwitz, Husain, Vergin, Isenman, Lee, Shakow, Holsen, Rao, Burmester/Thahane, Colliou, Steer, Baudon, Baudouy

For Information Only

cc: Messrs./Mmes Hopper, Frank, Parmar, Goldberg, Bock, Pfeffermann, Baneth, Kavalsky, Haug, Tanaka, Robless/Lawrence, Agarwala

GS

GSicat:sb

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

890814009 1.

DATE: June 12, 1989

TO: Mr. Moeen A. Qureshi, Senior Vice President, OPNSV

FROM: Michael Gillette, Acting Vice President, AFRVP

EXTENSION: 34000

SUBJECT: ZAIRE - Social Sector Adjustment Credit (SSAC) Initiating Memorandum

1. Through the attached Initiating Memorandum we are seeking approval by the Operations Committee to appraise the proposed Social Sector Adjustment Credit (SSAC).

Background

2. Recent economic developments in Zaire have been summarized in my memorandum to you of May 8, 1989 seeking the Operations Committee's approval of the release of the second tranche of the SAL I as well as submitting the final version of the second-year PFP and the Energy Sector Credit Initiating Memorandum.

3. Since May 8, the following events have occurred: (a) the second tranche of the SAL (US$82.5 million) was released on May 19, 1989; (b) Zaire repaid its arrears to the IMF; (c) the Operations Committee approved the Initiating Memorandum for the proposed IDA Energy Sector Credit of US$158 million including a US$90 million quick-disbursing component on May 26; and (d) the second-year PFP was considered by the Committee of the Whole on June 6 and by the IMF Board on June 9; this is expected to lead to the IMF making available a second SAF of SDR 87.3 million and a stand-by of SDR 116.4 million.

Bank Strategy for Support to Balance-of-Payment

4. With the adjustment program back on track we are following a two-pronged strategy: first, ensure that the program stays on track by monitoring it closely and leveraging performance through macroconditionality of sector adjustment operations; secondly, within the framework of the SPA mobilize sufficient resources to ensure the sustainability of the program and prevent a recurrence of the underfunding that was partly responsible for the abrupt end to the earlier phase of the reform program in 1983-1986. IDA will contribute its share of the overall financing requirements through quick-dibursing components of SECALs and hybrids before the SAL II is prepared in FY91. The vehicles we envisage for conditionality leveraging and resource transfers include the Energy Sector Credit, the Financial Sector Credit and the SSAC.

SSAC

5. In this context, the concept of the SSAC is similar to that of the Energy Sector Credit. It is a hybrid operation consisting of a policy component supporting quick disbursements (linked to both macroeconomic and sectoral performance) and a traditional investment component. In both cases, the justification of the quick-disbursing component is directly linked to macroeconomic performance and overall balance of payment support needs.

6. The SSAC policy component follows and complements the measures initiated by SAL I, with a specific focus on human resources. The two main elements of the SSAC package, PEP restructuring and non-governmental sector promotion, are closely linked to macroeconomic adjustments. First, adequate resource allocation to social sectors through the PEP process implies a major reorientation of Government expenditure within an acceptable macro ceiling to be negotiated/monitored jointly by the Government, IMF and the Bank. SSAC implementation will be closely associated with PERs and PFP implementation reviews. This joint macro/sectoral approach is necessary since the SSAC envisages a 50 percent increase in the share of social sectors in overall Government recurrent spending (from 12 percent to 18 percent in a three-year period); such large increase is required because of the drastic cuts that have taken place in recent years which have put the Zaire Government's social expenditures per capita at one of the lowest levels in Sub-Saharan Africa. Second, the promotion of increased participation by the private sector (including NGOs, private providers and beneficiaries) in social service delivery, is dependent upon the success of the stabilization program as defined in the PFP, because resource mobilization at the community level and conservation/improvement of consumer purchasing power are essential to sustain social services operating on a cost recovery basis. A third element of the policy package is to introduce new sectoral policies in education, health, nutrition and population. These policies, particularly those on population (on which there has been no policy so far), are expected to have major long-term benefits on economic growth; their introduction is specifically envisaged in the Government's April 1989 - March 1992 PFP. The proposed SSAC would provide further support to the Government to define these policies in more concrete, action-oriented terms.

7. In this perspective, the quick-disbursing component of the SSAC is similar to a supplement of the SAL I in that it is linked to specific macro conditionality (e.g. satisfactory implementation of the agreed public expenditure program, especially foreign expenditure by the Government, which will be monitored closely by Bank/Fund). On this basis it is proposed that the quick disbursing component be disbursed against a negative list of imports so as to provide the widest possible support to the balance of payments. Contrary to the Energy Sector Credit, which could disburse against sector-related imports (petroleum), such an approach is not possible for the SSAC because of the nature of the sector (small external financing gap).

8. The investment component (operational support to priority social programs) is justified because the social situation has been neglected for several years and requires certain quick and targeted actions to provide program support to the most vulnerable groups of population (including women and children). The largest part of that component will finance/cofinance selected priority programs, part of a three-year slice of the Government's PHN sector PIP, which has been reviewed and accepted by IDA in May 1989. No direct support to the Education sector PIP is provided in the SSAC because it is covered under a proposed Education Sector Rehabilitation Project, which is to be appraised shortly and for which the key policy conditionality (new sector strategy) is, however, entirely included in the policy component of the SSAC.

JBaudouy/AColliou/fd

cc: Messrs./Mss.: D. Hopper, E. Stern, S. Husain, A. Karaosmanoglu, W. Thalwitz, E. Jaycox (o/r), V. Rajagopalan, S. Fischer, I. Shihata, D.J. Wood, H. Vergin, M. Haug, J. Tanaka, L. Robless, A. Shakow (2), J. Holsen (3), V. Dubey, D. Lee, D.C. Rao, Burmester/Thahane, R. Liebenthal, A. Steer, T. Baudon, D. Bock, D. Goldberg, R. Frank, J. Parmar, G. Pfeffermann, J. Baneth, B. Kavalsky, A. Hamilton, B. Herz, A. Meesham, McGreevey, S. O'Brien, Aklilu Habte, S. Denning, C. Ohri, H. Wyss, R. Agarwala, P. Isenman, B. Varon, J.L. Sarbib, Ishrat Husain, J. Socknat, L. Christoffersen, N. Gorjestani, M. Blanc, A. Otten, M. Peñalver, S. Capoluongo, J. de Leede, P. Lazar, J. Chevallier (RMZ), U. Thumm, G. Sicat, T. Jones, M. Guerard, C. Ely-Hachana, Van der Mensbrugghe, Taplin (IMF).

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THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

890621003 1.

OFFICE MEMORANDUM

DATE: June 20, 1989

TO: Operations Committee

FROM: Vinod Dubey, Director, EAS

V Dubey

EXTENSION: 78051

SUBJECT: SAO TOME & PRINCIPE: Proposed Second Structural Adjustment Credit (SAC II) - Initiating Memorandum - Agenda

The Operations Committee will meet on Friday, June 23, 1989 at 12 noon in Room E-1243 to consider the IM for SAC II for the amount of US$9.5 million. This credit is to be disbursed in three tranches against general imports other than those in the negative list. This would be the second adjustment credit.

Rationale and Focus of SAC II

The first issue that the Committee might wish to consider is the rationale and focus of the proposed operation. SAC I was approved in mid 1987. Originally it was designed as a two tranche operation. However, because of slow implementation the second tranche was split into two, thereby creating a third tranche which is being considered for release now. The recently approved SAF program of the Fund concentrates on the exchange rate, balance of payments, monetary and banking and fiscal policies, including taxation policy reform. Progress has been impressive in these areas but mixed in others - especially those involving structural problems and requiring substantial implementation capacity. In a small (population: 115000) and very rudimentary economy, can the Bank contribute much by stressing the same macro management problems as the Fund or should it address issues in the real sectors, and strengthen infrastructure and implementation capacity to stimulate a supply response in the economy?

A related question pertains to the public investment program. In the past, the public investment program failed to contribute to economic growth and expanded the country's external debt beyond manageable limits. How does the Region propose to ensure that the public investment program which figures prominently in SAC II would prove to be a more productive and efficient vehicle for growth with stability than that in the past?

Agricultural Diversification, the Cocoa subsector and Land Distribution

In a country that has relied so heavily on a single crop, cocoa, and on estate-type production with the resultant discouragement to small holders and heavy dependence on imported food, are not the issues of agricultural diversification and efficient cocoa production the central ones? What concrete steps are being taken to diversify the agricultural sector? What crucial elements of the country's infrastructure are lacking? In addition to addressing many infrastructure deficiencies how can the Social Infrastructure Fund (SIF) also be an effective vehicle for developing private

entrepreneurship? What is the scope for fisheries and how best can it be developed? How is the cocoa producer price related to the international price and does it provide incentives for replantation/enhanced pickings? Is the land distribution policy likely to be effective and would it significantly contribute to shift of resources towards the private sector?

Realism in Projections

During 1984-87, GDP growth has been very weak and erratic. It seems to have picked up in 1988-89 but is it realistic to assume that a growth rate of 6-7% p.a. can be achieved on a sustainable basis particularly when the share of the public sector in total investment (96-97%) remains overwhelmingly dominant and budgetary revenues are expected to decline from about 20% of GDP during 1988-90 to 16% in 1991-93? With inflation over 25%. is it realistic to achieve positive real interest rates by end 1989?

Clarification in conditionality

In general it would be desirable to further refine and specify "satisfactory progress" by either giving benchmarks or criteria and clearly differentiating between the second and third tranche release conditions: e.g. IIc, IIIc and IIf and IIIf so that they are not subject to varying interpretations at the time of tranche releases.

Operations Committee

Messrs. Qureshi, Husain, Jaycox, Karaosmanoglu, Thalwitz
Rajagopalan, Fischer, Shihata, Wood, Vergin

cc: Messrs. Lee, Shakow, Holsen, Rao, Burmester/Thahane, Liebenthal, Steer, Baudon, Hopper, Bock, Goldberg, Kavalsky, Parmar, Pfeffermann, Baneth, Robless, Ms. Haug, Tanaka, Koch-Weser, Adams, Ms. O'Connor Fretes-Cibels

FMChaudhri:gs

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION 890620002 1. Mr Qureshi

OFFICE MEMORANDUM

DATE: June 19, 1989

TO: Mr. Moeen Qureshi, Senior Vice President, Operations

FROM: Mr. Edward V.K. Jaycox, Vice President, Africa Region 6/19

EXTENSION: 3400

SUBJECT: Sao Tome and Principe - Proposed Second Structural Adjustment Credit
Initiating Memorandum (IM)

Through the attached Initiating Memorandum (IM), we are seeking approval of the Operations Committe to appraise a proposed Second Structural Adjustment Credit to Sao Tome and Principe in the amount of US$9.5 million equivalent.

Attachement

Distribution

Operations Committee:	Messrs.	Husain, Karaosmanoglu, Thalwitz, Fischer, Shihata, Wood, Vergin
	Messrs.	D. Lee, Dubey, Shakow, Holsen, D.C. Rao, Burmester/Thahane, Liebenthal, Steer, Baudon
For Information:		Messrs. Hopper, Bock, Goldberg, Frank, Parmar, Pfeffermann, Baneth, Robless, Agarwala, Ms. Haug

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