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Sudan: Staff Report for the 2000 Article IV Consultation and Fourth Review of the First Annual Program Under the Medium-Term Staff-Monitored Program

This report was prepared by a staff team of the International Monetary Fund following discussions with the officials of Sudan on economic developments and policies. The report was then considered by the IMF's Executive Board in the context of the IMF's periodic consultation with Sudan, as required under Article IV of the IMF Articles of Agreement. The views expressed in the staff report itself are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF or of the authorities of Sudan; a supplementary statement by IMF staff may also be included. The views of the Executive Board as expressed in the discussion of the Article IV consultation report and as summarized in a Public Information Notice (PIN) are also included. In addition, a statement by the member country authorities may be appended. Further background documentation prepared by IMF staff for the consultation may be published separately at a later date. The policy of publication of Article IV staff reports allows for the deletion of market sensitive information.

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INTERNATIONAL MONETARY FUND

SUDAN

**Staff Report for the 2000 Article IV Consultation
and Fourth Review of the First Annual Program
Under the Medium-Term Staff-Monitored Program**

Prepared by Middle Eastern and
Policy Development and Review Departments

(In consultation with Fiscal Affairs, Legal, Monetary
and Exchange Affairs, Statistics, and Treasurer's departments)

Approved by Paul Chabrier and Thomas Leddy

May 8, 2000

- The staff teams included Mr. Zavadjil (head), Ms. Creane, Messrs. Al-Gebreen, Kireyev, Mahyoub (all MED), and Arvanitis (PDR).
- The staff team met with His Excellency Mohammed Kheir El Zubeir, Minister of Finance and National Economy; His Excellency Saber Mohammed Hassan, Governor of the Bank of Sudan, and other senior Sudanese officials, as well as private sector and diplomatic representatives.
- The principal authors of the report were Milan Zavadjil, Susan Creane, Alexei Kireyev and Athanasios Arvanitis.

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EXECUTIVE SUMMARY

Performance under the program

- The objectives of the 1999 SMP were broadly achieved although, as anticipated, the macroeconomic situation at the end of 1999 was modestly more expansionary than programmed. Central bank financing of the fiscal deficit and inflation were both slightly above program, and while targets for growth of broad money and net domestic credit were met, the increase in reserve money was significantly above projections. The exchange rate remains roughly unchanged and early data indicate that the 2000 macroeconomic program is on track.
- Previously delayed structural reforms are moving forward. The tax authority is vigorously pursuing the last steps required ahead of the June 1 start date for the VAT. Implementing regulations for the Investment Encouragement Act have now been passed which go beyond previous expectations in closing import tax loopholes. The other remaining fiscal and monetary reforms for end-1999 are now completed. Measures committed for early 2000 have been taken.

Policy discussions

- Given general agreement that the overall program is broadly on track, the main issues are sustaining and improving the current macroeconomic conditions, implementation of the structural reform agenda without further delays, and the macroeconomic impact of the emerging oil sector. The decline in credit to the private sector in 1999 was noted and the authorities pledged several measures to address it. The program's structural agenda has now largely caught up with earlier delays. However, although agreement has been reached on a formula for automatic adjustments to maintain domestic petroleum product prices at international levels, the adjustments are not being implemented as needed.
- Regarding payments to external creditors, the authorities reaffirmed their commitment to return payments to the Fund to US\$60 million in 2000 and to resume payments to other external creditors, including the World Bank, at previously agreed levels. Sudan's efforts to normalize relations with the other creditors continue to show success.

Staff appraisal

- The MTSMP was broadly on track through end-1999 and appears to be continuing well through early 2000. The somewhat expansionary macroeconomic stance and difficulties in bringing inflation into the single digits underscore the need for keeping to program targets and tightening further as necessary. The stability in the nominal exchange rate for the past 9 months is also a cause for concern. The authorities are urged to push ahead without further delay on the remaining structural reform agenda, especially with regard to petroleum product prices. The continuing improvement in relations with external creditors is welcomed.

I. INTRODUCTION

1. **Focus of the report.** Discussions on the 2000 Article IV consultation and Sudan's performance under the fourth quarterly review of the first annual program under the medium-term staff-monitored program (MTSMP) took place in Khartoum during March 25–April 9, 2000. This report presents the mission's findings on economic performance through end-1999, the outcome of the 2000 Article IV discussions, and the objectives and policies for the remainder of 2000 under the MTSMP, as described in the attached Letter of Intent and Memorandum of Economic Policies addressed to the Managing Director and dated May 7, 2000.
2. **Fund and World Bank Relations.** Sudan has Article XIV status. Relations with the Fund and the Bank are summarized in Appendices I and II.
3. **Directors' views.** On February 28, 2000, the Executive Board considered the Third Review of the First Annual Program and the Program for 2000 under the MTSMP, EBS/00/22, (2/14/00), and also gave further consideration to the Managing Director's complaint with respect to compulsory withdrawal. At that time, the Board welcomed the adoption by the Sudanese authorities of a program of economic and financial adjustment for 2000 consistent with the key parameters of the MTSMP. The authorities were urged to take all necessary actions to implement the program fully, including by maintaining appropriately tight fiscal and credit policies and implementing key structural reforms. The Board further agreed to give consideration within six months' time to lifting the suspension of Sudan's voting and related rights in the Fund.
4. **Political situation mixed.** Sudan's efforts to normalize political and financial relations with the international community continue. A senior U.S. official was in Khartoum in March to meet with the government, the first to visit Sudan since 1998, while high-level contacts with neighboring countries are expanding. Following the March extension of the state of emergency through end-2000, the timing of the proposed reconciliation conference with the opposition which is slated to pave the way for new elections has not yet been scheduled. The prominent Umma political party, headed by the former Prime Minister El-Mahdi, has broken off from the alliance of opposition groups and returned to Khartoum after a decade's absence for discussions with the government. However, despite meetings under International Governmental Authority for Development auspices between the government and the Sudan Peoples' Liberation Army, no progress is being made in the peace process, and conflicts between government and armed opposition forces continue.

II. BACKGROUND

5. **After decades of stagnation and instability, encouraging signs of economic progress along with continuing challenges.** During the last three years under staff monitored programs, Sudan made progress in reducing macroeconomic imbalances and in beginning to dismantle an interventionist government policy structure, contributing to the

solid economic growth (averaging about 6 percent) achieved in the last third of the 1990s (see Table 1).¹ This progress was achieved against the background of several natural disasters, a civil conflict, and net outflows on the official capital account. Together with the recent thaw in relations with neighboring countries, the Arab world, and to some extent the EU, as well as the onset of oil production, it raises hope that the improvement in economic performance can be sustained. However, despite the relatively strong economic growth in recent years, much of the Sudanese population remains mired in poverty and overall social indicators are weak (Table 2).

6. **Long-term risks for Sudan's macroeconomic outlook.** Looking ahead, obstacles to future growth persist—many of which were outlined in the 1999 Article IV Staff Report. The new revenues from oil provide a welcome boost to budget resources but will not on their own be able to sustain the required increase in development and social spending, while public expectations and political pressures for immediate visible use of oil revenues are rising. Sudan has large tracts of arable land, but the deteriorating infrastructure, recurrent problems with flooding, an inappropriate institutional framework in the irrigated sector, and a secular decline in world commodity prices, have undermined the agricultural sector—which through the 1990's has been the most important source of economic growth (Box 1). The fragile and undercapitalized banking system does not appear capable of supporting private sector growth, and is constrained by an outdated legal system. The public enterprise sector is small but still inefficient, and privatization is constrained by the poor state of most enterprises and limited domestic or foreign interest. Investment in physical and human capital remains low. The civil service is strong in relation to comparator countries and most of the key decision-makers seem committed to reform, although overall administrative capacity is still low and the civil service underpaid. While the authorities recognize the need to limit military spending particularly in light of competing budgetary needs, further spending pressures will continue—including possibly for demobilization. Finally, Sudan's external debt, estimated at US\$24 billion at end-1999 is immense. Any eventual resolution is likely to be complicated and time consuming and there is a growing domestic perception that Sudan might make better use of its new foreign exchange earnings for purposes with near-term productive results rather than debt service to non-disbursing creditors.

III. RECENT DEVELOPMENTS AND PROGRAM PERFORMANCE THROUGH END-1999

A. Macroeconomic Developments

7. **The macroeconomic objectives of the 1999 SMP were broadly achieved.** Grounded in solid growth in agriculture (mainly in livestock, and the rainfed and non-traditional crops sectors) and boosted by the start-up of oil production mid-year, real growth is estimated at about 6 percent in 1999, continuing the trend of recent years (Table 1).

¹Initial steps toward liberalization were taken from 1993, but accompanied by macro-economic instability.

Table 1. Sudan: Selected Economic and Financial Indicators, 1997–2000

	1997	1998	Prog. December 1999	Actual	Prog. December 2000	Proj.
(Annual changes in percent)						
National income, production, and prices						
Nominal GDP (in billions of Sudanese dinars) 1/	1,615	1,986	2,357	2,443	2,811	2,914
Real GDP growth	6.7	5.0	6.0	6.0	6.5	6.5
End-of-period CPI inflation	32.0	7.9	10.0	17.0	9.0	9.0
Average CPI inflation	46.7	17.1	14.0	16.0	12.0	12.0
(In percent of GDP)						
Investment and saving						
Gross investment	16.5	17.6	16.2	16.7	17.4	17.4
Public sector	0.6	0.8	1.6	1.3	2.3	2.3
Private sector	15.9	16.8	14.6	15.4	15.0	15.1
Saving	9.8	7.7	12.1	13.2	15.1	16.1
Public sector	-0.2	0.1	0.5	0.4	1.3	2.3
Private sector	9.9	7.6	11.5	12.8	13.8	13.8
Central government operations						
Total revenue	6.6	7.9	8.8	8.5	10.8	11.5
Total expenditure	7.4	8.6	9.8	9.3	11.9	11.5
Overall balance (cash)	-0.7	-0.7	-1.0	-0.9	-1.1	0.1
(Changes in percent of beginning broad money stock)						
Money and credit 2/						
Net foreign assets (excluding valuation changes)	17.4	15.4	14.4	7.3	9.7	8.5
Net domestic assets	19.6	14.1	9.2	17.3	9.7	10.9
Net domestic credit, of which:	15.0	12.9	8.7	5.8	9.1	9.1
Net claims on central government	9.3	6.7	4.8	4.7	3.3	3.3
Claims on nongovernment sectors	6.7	3.9	4.8	2.1	5.8	5.8
Other items (net)	4.5	1.3	0.5	11.5	0.6	1.7
Broad money	37.0	29.6	23.6	24.6	19.4	19.4
Reserve money (change in percent)	34.3	29.4	19.7	35.1	19.2	17.1
Velocity (GDP/average broad money)	11.6	10.7	10.1	10.3	9.9	10.1
(In millions of U.S. dollars, unless otherwise indicated)						
External sector						
Exports, f.o.b.	594	596	729	780	1,252	1,373
Imports, c.i.f.	-1,580	-1,925	-1,549	-1,412	-1,366	-1,317
External current account balance 3/	-330	-338	-349	-236	-201	-150
In percent of GDP	-4.0	-3.9	-3.0	-2.4	-2.0	-1.3
Terms of trade (change in percent) 4/	-4.4	5.2	-4.8	0.2	-3.1	2.8
Real effective exchange rate (eop, change in percent)	22.0	-25.8	...	18.8	...	...
Official exchange rate (end of period, SD/US\$)	172	237	...	256	...	...
Total external debt service (percent of current receipts)						
Commitment basis	97.4	93.1	82.6	83.1	64.5	60.9
Actual payments	4.7	4.6	2.8	4.2	4.5	5.1
External debt (billions of US\$)	21.3	22.5	23.6	23.7	24.9	24.9
BOS gross usable reserves (millions of US\$)	...	27.0	47.0	53.4	92.0	211.3
In months of imports	...	0.2	0.4	0.5	0.8	2.0
As percent of short-term debt 5/	...	40.1	67.1	76.0	54.8	112.4

Sources: Fund staff estimates and projections based on information provided by the Sudanese authorities.

1/ 1997–98 revised by Central Bureau of Statistics.

2/ Reflects reclassification in December 1999 of old claims on the government (see Table 4).

3/ Excluding interest due, public transfers, and oil pipeline imports.

4/ Non-oil transactions.

5/ Includes short-term debt, and actual debt service payments (to the Fund and other creditors).

Table 2. Sudan: Demographic, Social and Education Indicators

		Sudan				Average for Sub-Saharan Africa
	Units	1996	1997	1998	1999	1997
Demographic indicators						
Population	Millions	27.9	28.7	29.4	30.3	...
aged 0-14	Percent of total	44.1	44.1	44.1	43.7	44.5
aged 15-64	Percent of total	53.5	53.5	53.5	53.9	52.3
aged 65 and above	Percent of total	2.4	2.4	2.4	2.4	2.9
Population growth	Percent, 1993-98 average	2.7	2.7	2.6	2.6	2.8
Population gender balance	men/women	101	101	101	101	...
Age dependency	Ratio 1/	87	87	87	86	90
Urban population	Percent of total	30.1	30.3	30.6	33.1	32.3
Social indicators						
Total labor force	Millions	8.9	9.2	9.4	9.7	...
male	Percent of total labor force	44.8	44.6	44.7	44.7	57.8
female	Percent of total labor force	55.8	55.5	55.7	55.6	42.2
Participation rate	Percent	32.1	32.1	32.1	32.1	...
Life expectancy at birth	Years	55.3	55.7	56.1	56.5	50.8
male	Years	53.8	54.2	54.6	55	49.4
North	Years	54.8	55.3	55.7	56.1	...
South	Years	47.2	47.6	48	48.4	...
female	Years	56.7	57.1	57.5	57.9	52.3
North	Years	57.9	58.3	58.7	59.1	...
South	Years	49.9	50.3	50.7	51.2	...
Infant mortality rate	Per 1,000 live births	...	71.0	...	...	91.4
Access to safe water 2/	Percent	60.0	...	...	...	...
urban	Percent	84.0	...	...	...	...
rural	Percent	41.0	...	...	...	...
Immunization rate	Percent under 12 months	80.3	94.0	...	...	...
measles	Percent under 12 months	75.0	92.0	63.2	...	57.9
DPT	Percent under 12 months	80.0	79.0	87.5	...	52.6
Education indicators						
Adult literacy rate	Percent	53.5	...	57.2	...	58.3
male	Percent	67.1	...	67.3	...	66.5
female	Percent	39.8	...	47.1	...	50.4
Primary education (1995/96 and 98/99)						
Pupils	Thousands	2864	...	2977	...	...
	Percent female	45.1	...	46.0	...	...
Teachers	Thousands	94	...	103	...	...
	Percent female	60.0	...	71.3	...	...
Ratio of pupils to teacher		31	...	31	...	41 3/
Secondary education						
Pupils	Thousands	341	...	642	...	...
	Percent female	46.3	...	...	...	...
Teachers	Thousands	12	...	14	...	...
	Percent female	44.3	...	...	...	...

Sources: Central Bureau of Statistics, Ministry of Finance and National Economy; and World Bank's World Development Indicators.

1/ Population under the age of 15 and over the age of 65 as a share of the total working-age population.

2/ 1995 data.

3/ 1994 data.

Box 1. Sudan: Sources of Growth—Past and Future

Real growth has expanded at an average 5 percent throughout the 1990's, but at a higher average 6 percent growth rate since the start of the staff-monitored programs in 1997. Through the years the agriculture sector has maintained its primary importance in the economy, accounting for about 40 percent of total GDP. Given its heavy weight on the economy, developments in agriculture have an obvious important impact on the outcome for overall real growth in the economy, as can be seen in the developments in 1996 when drought affected the rainfed crops. In recent years, traditional crops—particularly in the irrigated sector—have become less important sources of growth than nontraditional crops and livestock. Outside of the diversification taking place within the agricultural sector, the other major new source of growth is from the onset of oil production.

Contribution to Growth by Sector

	1992/93	1993/94	1994/95	1996	1997	Est. 1998	1999	Proj. 2000
(Annual percentage change)								
Growth rate	3.8	1.8	8.9	4.0	6.7	5.0	6.0	6.5
Share explained by:								
(Percent of total growth)								
Agriculture	-5.8	202.9	33.4	-49.3	92.4	79.1	46.0	9.4
Crops	-142.7	192.8	20.8	39.8	45.7	75.5	22.9	-5.4
Traditional crops	-5.8	-162.7	54.3	-54.1	54.5	-38.8	-1.7	-21.9
Irrigated	-47.2	-17.1	7.5	4.2	13.1	-14.8	-29.0	8.4
Rainfed	41.4	-145.6	46.8	-58.3	41.4	-24.0	27.3	-30.3
Other crops	-136.9	355.5	-33.5	93.9	-8.8	114.3	24.6	16.5
Livestock	192.2	54.1	24.9	-81.8	49.6	3.6	22.9	15.3
Forestry	-55.4	-44.0	-12.3	-7.3	-2.9	0.1	0.3	-0.5
Manufacturing and mining 1/	-16.2	-7.6	20.2	88.2	1.7	10.8	18.8	58.0
Construction	8.4	77.4	-20.7	35.5	35.3	1.4	2.2	32.2
Other	113.6	-172.8	67.1	25.6	-29.4	8.7	33.0	0.4

Sources: Sudanese authorities and Fund staff estimates.

1. Includes oil sector.

There is considerable economic literature on the determinants of growth, with general agreement on the importance of certain key factors, including high investment, low inflation, and strong social indicators—such as for education. For very rough comparison purposes, the table below sets out current indicators for Sudan against data indicating variables associated with some fast-growing economies.

Factors Affecting Growth 1/

	Fast-growing economies	Slow-growing economies	Sudan 2/	
			1996	1999
(In percent)				
Primary school enrollment rate	90	54	56	61
Secondary school enrollment rate	30	10	34	...
Share of investment in GDP	23	17	15	17
Average annual inflation rate	12	31	133	16
Share of exports to GDP	32	23	8	8
Share of government consumption in GDP 3/	16	12	10	9

1. Sources: Fischer, Sahay and Vegh (1998) IMF WP/98/52. Sudanese authorities and Fund staff estimates.

2. Sudan's economic adjustment program began in earnest in 1997.

3. There is no consensus regarding the direction of the effects of government consumption on growth; the impact depends on the type and quality of government spending, and its financing.

Inflation, which had been on a declining trend, experienced a year-end flicker upward to 17 percent due in part to higher than anticipated spending pressures in Ramadan and ahead of the Eid-al-Fitr holiday in January, and in part to the rise in sorghum prices as a result of lower production compared to one year earlier. The result was an average inflation rate for the year of 16 percent, somewhat exceeding the 14 percent program target.

8. **Modestly more expansionary than programmed overall macroeconomic policy stance.** Budget expenditure was maintained below the program level throughout the year and a surge in oil prices in late 1999 increased oil revenue above budgeted amounts (Table 3 and Chart 1). However, these were not sufficient to fully offset shortfalls in non-oil revenue (customs revenue fell short due to lower than expected imports in the fourth quarter), emergency expenditure earlier in the year following flooding, and lower than expected foreign financing inflows. As a result, while the overall fiscal deficit, at 0.9 percent of GDP, was less than targeted under the program, net domestic financing of the fiscal deficit was slightly above target (by 0.1 percent of GDP).

9. **Broad money growth at end-December was roughly in line with the 1999 program** (Table 4). While credit to government exceeded the benchmark level, credit to private sector was sharply lower than programmed, falling during the year (Charts 2–3). As a result, the benchmark on net domestic credit of the banking system was met (Appendix III, Table 1). However, net domestic assets of the banking system exceeded the indicative benchmark substantially partly due to the higher than envisaged government borrowing and partly due to an unexpected rise in net assets caused by unprogrammed increases in the accounting entries for the accrued interest on government debt done at end-December for the year as a whole (paragraph 42 below), repayment of some Agricultural Bank debts by the BOS and, to smaller degree, for not as yet fully explained reasons.² Reserve money significantly exceeded the expected level for end-1999, fueled by stronger than expected seasonal transaction demand for currency in December associated with Ramadan (Table 5). After some depreciation in the first half of 1999, the exchange rate has remained broadly stable in nominal terms. Against the background of generally declining inflation and nominal exchange rate stability, the real effective exchange rate appreciated through end-year by 19 percent; although on a year-average basis, the real exchange rate depreciated in 1999 over 1998 (Chart 4).

10. **Gross official reserves above target level.** Higher than expected oil export prices helped to offset the weak performance of traditional exports, resulting in a better than programmed outcome for the current account deficit (excluding interest due and public transfers) at 3.5 percent of GDP (Table 6). The Bank of Sudan (BOS) closed the year by

²These may be due to remaining small discrepancies between the central bank's claims on commercial banks and commercial banks' claims on the central bank, and are being addressed by a STA technical assistance mission now in the field (paragraph 38).

Table 3. Sudan: Central Government Budget, 1997-2000

	1997	1998	1999		2000	
			Program	Actual	Program 1/	Staff Proj.
(In billions of Sudanese dinars)						
Total revenues	107.3	156.9	206.5	206.7	304.2	335.9
Tax revenue	90.9	126.4	156.9	153.3	193.7	193.6
Direct taxes	21.7	31.2	38.1	36.1	46.8	46.7
Indirect taxes	69.2	95.2	118.8	117.2	146.9	146.9
On international transactions	48.2	69.3	86.7	84.4	67.8	84.9
On domestic transactions	21.0	25.9	32.0	32.8	33.6	39.3
VAT	0.0	0.0	0.0	0.0	45.5	22.8
Non-tax revenue	16.4	30.4	49.6	53.4	110.5	142.3
Departmental fees	6.3	9.5	11.5	9.4	15.3	15.3
National revenues	10.1	21.0	38.1	44.0	95.3	127.0
of which: sales of crude oil 2/	0.0	0.0	7.6	15.7	63.6	95.3
Total expenditure	119.1	170.9	231.0	228.4	333.9	333.9
Current expenditure	109.8	155.3	194.4	196.2	268.0	268.0
Wages 3/	37.5	57.3	81.6	80.4	105.6	105.6
Goods and services	45.8	31.2	36.9	37.9	60.7	60.7
Transfers to states 4/	4.7	8.9	21.8	12.8	25.1	25.1
Debt service 5/	10.1	13.9	16.3	20.2	27.6	29.5
Other	11.7	44.0	37.9	44.9	49.0	47.1
Capital expenditure	9.3	16	36.7	32.2	65.9	65.9
Domestic financed, of which:	6.7	12	29.1	25.7	48.0	48.0
Repayment of oil sector loans 6/	...	...	...	3.6	18.0	18.0
Other	6.7	12.2	29.1	22.1	30.0	30.0
Foreign financed	2.6	3.4	7.5	6.5	17.9	17.9
Overall deficit (cash basis)	-11.8	-14.0	-24.5	-21.7	-29.7	2.0
Financing	11.8	14.0	24.5	21.7	29.7	-2.0
Foreign financing	2.6	3.4	14.4	8.5	20.6	20.6
Domestic financing	9.2	10.6	10.0	13.2	9.1	-22.6
Central bank financing	9.4	10.6	7.5	12.8	8.0	-23.7
Borrowing from the central bank	8.0	8.9	7.5	12.1	8.0	0.0
Change in government deposits with BOS	-1.4	-1.7	0.0	-0.7	0.0	23.7
Other domestic financing	-0.2	0.0	2.5	0.4	1.1	1.1
Memorandum items						
Military expenditure	...	42.8	63.1	62.2	84.1	84.1
Social expenditure	...	...	42.1	40.9	59.2	59.2
(In percent of GDP)						
Total revenues	6.6	7.9	8.8	8.5	10.8	11.5
Sales of crude oil	0.0	0.0	0.3	0.6	2.3	3.3
Non-oil revenue	6.6	7.9	8.4	7.8	8.6	8.3
Total expenditure	7.4	8.6	9.8	9.3	11.9	11.5
Current expenditure	6.8	7.8	8.2	8.0	9.5	9.2
Debt service	0.6	0.7	0.7	0.8	1.0	1.0
Non-debt service	6.2	7.1	7.6	7.2	8.6	8.2
Capital expenditure	0.6	0.8	1.6	1.3	2.3	2.3
Overall deficit (cash basis)	-0.7	-0.7	-1.0	-0.9	-1.1	0.1
Financing	0.7	0.7	1.0	0.9	1.1	-0.1
Foreign financing	0.2	0.2	0.6	0.3	0.7	0.7
Domestic financing	0.6	0.5	0.4	0.5	0.3	-0.8
Of which: Central bank financing	0.6	0.5	0.3	0.5	0.3	-0.8

Sources: Sudanese authorities and Fund staff estimates.

1/ Based on original 2000 GOS budget.

2/ The authorities 2000 budget is based on an oil export price of US\$15.75 per barrel, while staff projections are based on the WEO-consistent oil price of US\$21.5 per barrel (February 2000).

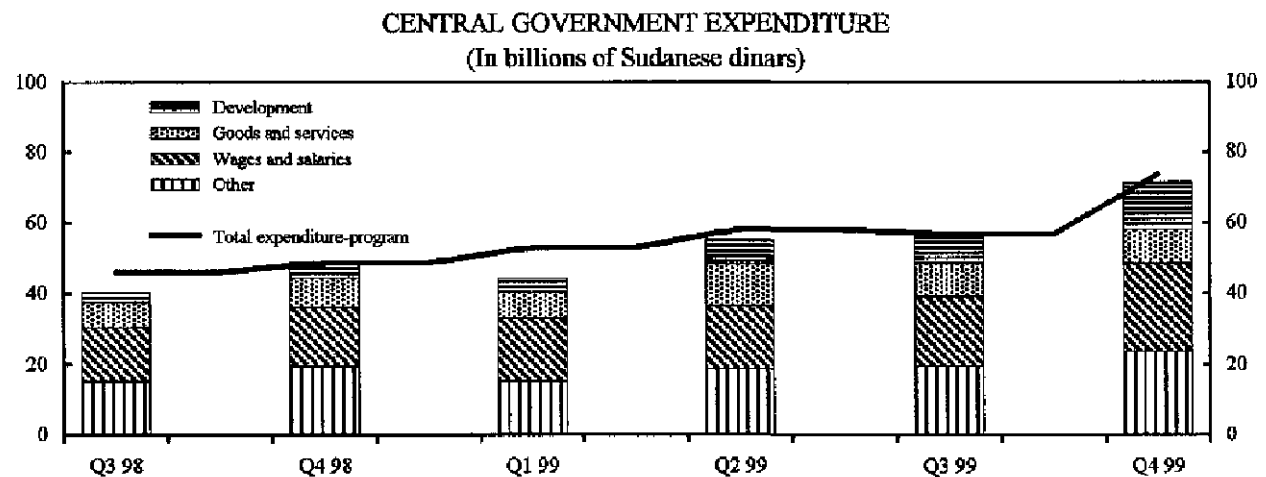
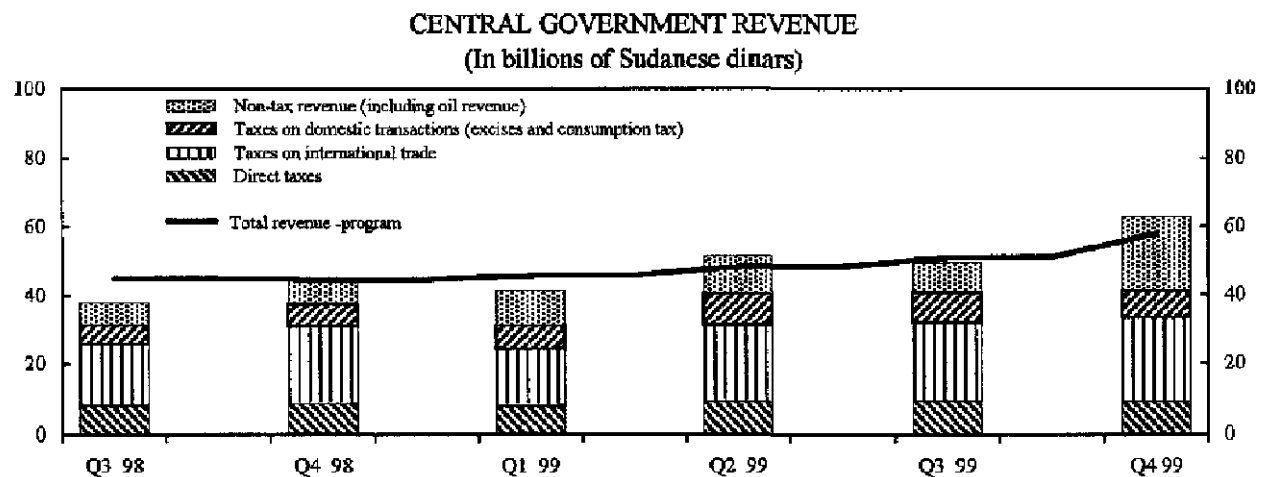
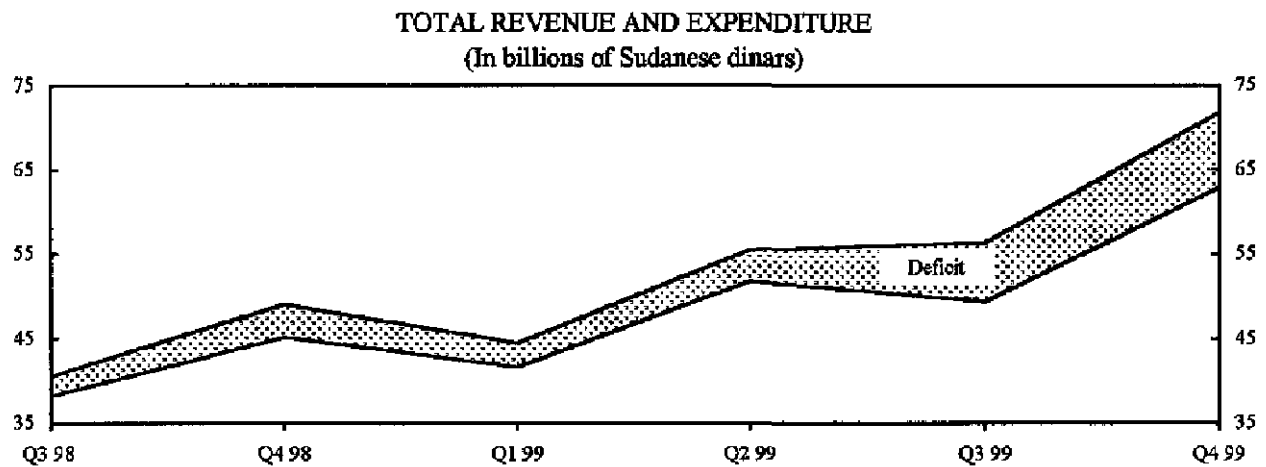
3/ Includes wages, salaries, pension and social insurance.

4/ Includes current and capital expenditure.

5/ Includes all actual payments, including interest, amortization and arrears repayments.

6/ Repayments of loans to foreign partners who financed the Sudanese equity share in the refinery and the pipeline.

CHART 1. SUDAN: FISCAL DEVELOPMENTS



Source: Sudanese authorities; and IMF estimates.

Table 4. Sudan: Monetary Survey, 1997–2000

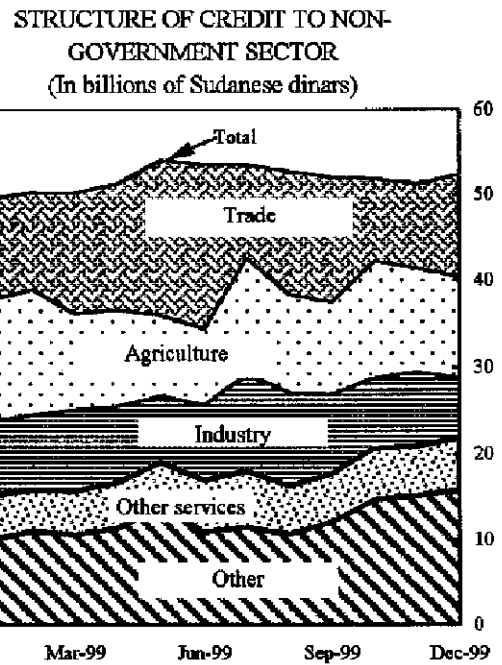
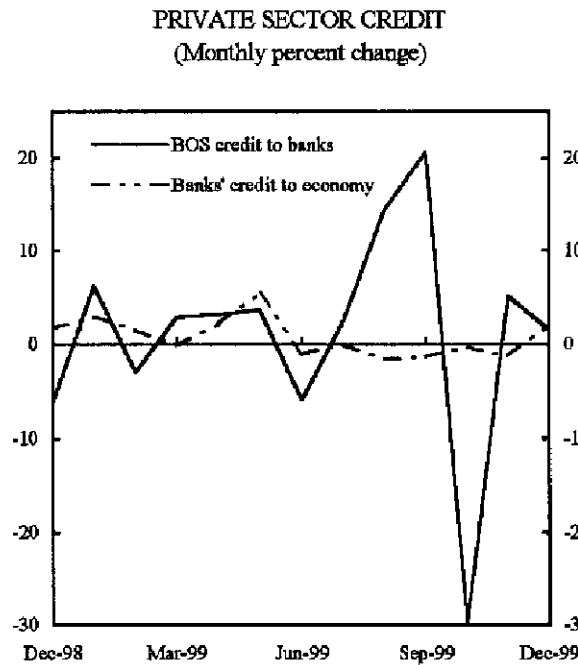
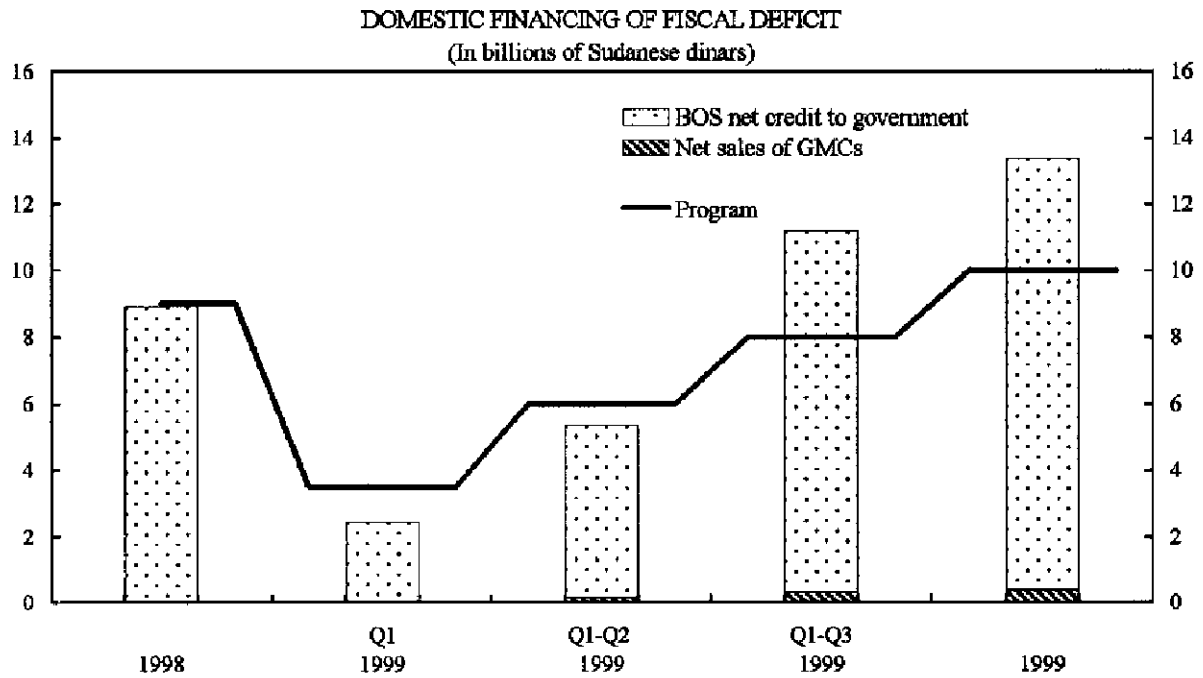
	Actual				Program	2000 Program			
	Dec.	Dec.	Dec.	Dec.	Dec.	Mar.	June	Sept.	Dec.
	1997	1998	1999		1999	2000			
			Old	Rev. 1/					
(In billions of Sudanese dinars)									
Net foreign assets	-493.6	-685.5	-726.4	-726.4	-739.3	-727.5	-726.0	-722.6	-717.8
Bank of Sudan	-533.7	-744.7	-791.5	-791.5	-809.4	-793.5	-792.8	-790.8	-787.4
Foreign assets	14.0	21.5	48.6	48.6	28.8	48.9	51.7	55.9	61.5
Foreign liabilities 2/	-547.7	-766.3	-840.1	-840.1	-838.3	-842.4	-844.6	-846.7	-848.9
Commercial banks	40.1	59.2	65.1	65.1	70.1	66.0	66.8	68.2	69.6
Counterpart to valuation changes 2/	530.1	746.6	802.6	801.2	830.2	804.6	807.9	811.3	814.7
Net domestic assets	123.2	145.8	181.7	183.1	164.8	192.6	199.8	206.7	211.1
Net domestic credit	99.2	119.8	131.8	151.2	137.8	160.1	165.5	171.4	174.7
Net claims on central government 3/	62.4	73.1	82.8	102.3	83.1	105.4	107.5	109.6	110.8
Bank of Sudan	62.8	73.4	86.2	105.6	80.9	108.6	110.6	112.6	113.6
Gross credit to government	66.8	75.7	87.8	107.3	83.2	110.3	112.3	114.3	115.3
Deposits of central government	4.0	2.3	1.6	1.6	2.3	1.6	1.6	1.6	1.6
Commercial banks 3/	-0.4	-0.3	-3.4	-3.4	2.2	-3.2	-3.1	-3.0	-2.9
Deposits of public enterprises at BOS	0.9	0.3	1.7	1.7	0.9	1.7	1.7	1.7	1.7
Deposits of other public entities at BOS	4.3	1.1	1.8	1.8	2.5	1.8	1.8	1.8	1.8
Claims on nongovernment sectors	41.9	48.1	52.4	52.4	58.1	58.1	61.4	65.2	67.4
Other items (net)	24.0	26.0	49.9	31.9	27.0	32.6	34.4	35.4	36.4
Broad money	159.7	206.9	257.9	257.9	255.7	269.7	281.8	295.4	307.9
Currency outside banks	58.5	82.1	108.1	108.1	93.0	110.8	111.1	113.9	125.3
Demand deposits	88.0	105.2	126.3	126.3	130.3	140.3	149.6	158.9	158.3
in local currency	43.2	48.7	61.5	61.5	65.3	73.5	81.5	89.5	88.5
in foreign currency	44.9	56.5	64.8	64.8	65.0	66.8	68.1	69.4	69.8
Quasi-money deposits	13.2	19.6	23.5	23.5	32.4	18.6	21.1	22.6	24.4
Memorandum item									
NFA excluding valuation changes	36.5	61.1	76.3	74.8	90.9	77.0	81.9	88.7	96.9
(In percent)									
Monetary ratios									
Currency/local currency deposits	103.8	120.3	127.1	127.1	95.2	120.3	108.3	101.6	110.9
Currency/broad money	36.6	39.7	41.9	41.9	36.4	41.1	39.4	38.5	40.7
Foreign currency deposits/broad money	28.1	27.3	25.1	25.1	25.4	24.8	24.2	23.5	22.7
Net domestic credit/total deposits	98.0	96.0	88.0	101.0	84.7	100.8	97.0	94.4	95.6
Total deposits/broad money	63.4	60.3	58.1	58.1	63.6	58.9	60.6	61.5	59.3

1/ Reflects the reclassification in December 1999 of old claims on government from other items (net) into gross credit to the government. The 1999 program should be compared to the "old" 1999 column. The 2000 program has been revised to reflect the reclassification.

2/ The increase in the counterpart to valuation changes mainly reflects the change in the value of the BOS liabilities owing to exchange rate movements.

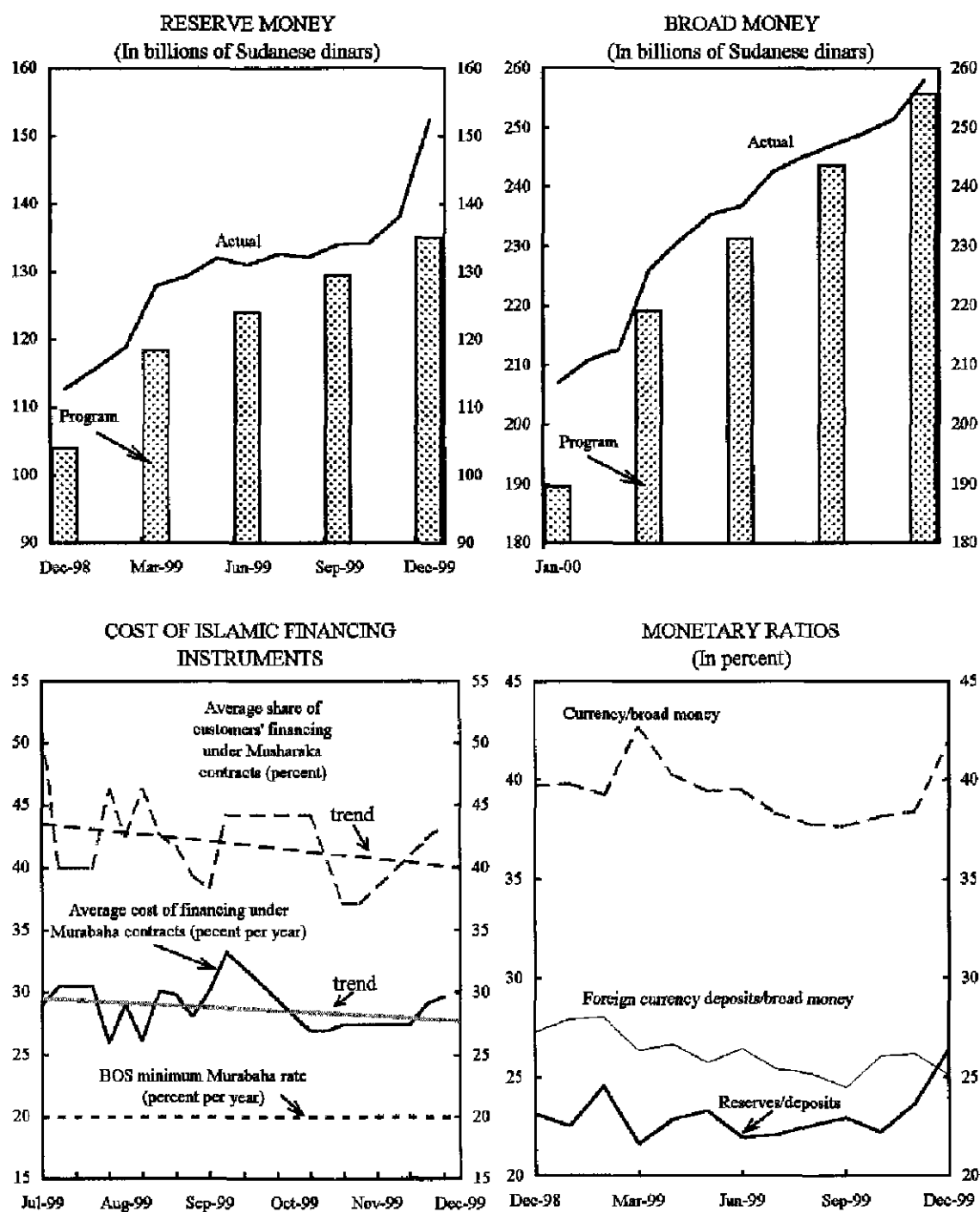
3/ Commercial banks net claims consist of deposits of public entities and local governments, in addition to central government deposits which in turn consist mainly of temporary end-month balances used to pay wages at the beginning of each month. Thus, as classified, changes in this item do not only reflect changes in commercial banks' net claims on the central government.

CHART 2. SUDAN: CREDIT DEVELOPMENTS



Source: Bank of Sudan.

CHART 3. SUDAN: MONETARY DEVELOPMENTS



Source: Bank of Sudan.

Table 5. Sudan: Monetary Authorities' Accounts, 1997-2000

	Actual				Program	2000 Program			
	Dec	Dec.	Dec.	Dec.	Dec.	Mar.	June	Sept.	Dec.
	1997	1998	1999	1999	1999	2000			
			Old	Rev. 1/					
(In billions of Sudanese dinars)									
Net foreign assets 2/	-533.7	-744.7	-791.5	-791.5	-809.4	-793.5	-792.8	-790.8	-787.4
Foreign assets	14.0	21.5	48.6	48.6	28.8	48.9	51.7	55.9	61.5
Foreign liabilities	-547.7	-766.3	-840.1	-840.1	-838.3	-842.4	-844.6	-846.7	-848.9
Counterpart to valuation changes	532.9	749.0	802.3	801.6	826.7	805.3	809.1	812.8	816.5
Net domestic assets	88.0	108.5	141.7	142.3	117.7	148.7	147.8	149.8	149.4
Net domestic credit	61.9	79.0	92.9	112.4	89.2	118.5	116.3	117.8	117.2
Net claims on central government	62.8	73.4	86.2	105.6	80.9	108.6	110.6	112.6	113.6
Claims on government	66.8	75.7	87.8	107.3	83.2	110.3	112.3	114.3	115.3
Deposits of central government	4.0	2.3	1.6	1.6	2.3	1.6	1.6	1.6	1.6
Central Bank credit to banks	4.0	7.8	8.8	8.8	13.5	13.0	8.8	9.3	9.8
Central Bank credit to public enterprises	0.2	0.2	3.5	3.5	0.2	3.5	3.5	3.5	3.5
Deposits of public enterprises at BOS	0.9	0.3	1.7	1.7	0.9	1.7	1.7	1.7	1.7
Deposits of other public entities at BOS	4.3	1.1	1.8	1.8	2.5	1.8	1.8	1.8	1.8
Banks' holdings of CMCs 3/	0.0	1.0	2.1	2.1	2.0	3.2	3.2	4.2	6.3
Other items (net)	26.1	29.5	48.8	30.0	28.5	30.2	31.5	32.0	32.3
Reserve money	87.2	112.8	152.4	152.4	135.0	160.5	164.0	171.8	178.5
Currency outside banks	58.5	82.1	108.1	108.1	93.0	110.8	111.1	113.9	125.3
Bank's reserves	26.9	28.9	39.7	39.7	40.1	44.8	47.6	52.3	47.4
Required reserves	11.7	16.1	22.6	22.6	20.2	22.7	24.5	26.2	26.1
On domestic currency deposits	11.3	13.1	18.6	18.6	17.0	14.7	16.3	17.9	17.7
On foreign currency deposits	0.4	3.0	4.0	4.0	3.2	8.0	8.2	8.3	8.4
Excess reserves	15.2	12.8	17.1	17.1	19.9	22.1	23.2	26.1	21.3
of which: cash in vault at commercial banks	5.1	4.3	5.8	5.8	3.9	6.3	6.6	7.4	6.1
Other deposits with the central bank	1.8	1.8	4.6	4.6	1.9	4.9	5.3	5.6	5.9
(Changes in percent of beginning reserve money stock)									
Net foreign assets	-95.2	-242.0	-41.5	-41.5	-57.4	-1.3	-0.9	0.5	2.7
Counterpart to valuation changes	106.5	247.9	47.2	46.6	68.9	2.4	4.9	7.3	9.8
Net domestic assets	23.0	23.5	29.4	30.0	8.2	4.2	3.6	4.9	4.7
of which: net claims on government	6.2	12.1	11.3	28.6	6.7	2.0	3.3	4.6	5.2
Reserve money	34.3	29.4	35.1	35.1	19.7	5.3	7.6	12.7	17.1
Currency outside banks	21.6	27.1	23.0	23.0	9.6	1.8	2.0	3.8	11.2
Bank's reserves	12.8	2.3	9.6	9.6	9.9	3.3	5.2	8.3	5.0
Required reserves	6.7	5.1	5.8	5.8	3.6	0.0	1.2	2.4	2.3
Excess reserves	6.1	-2.8	3.8	3.8	6.3	3.3	4.0	5.9	2.8
Memorandum items:									
NFA excluding valuation changes (Sudanese dinar billions)	-0.8	4.3	10.7	10.1	17.3	11.8	16.2	22.0	29.1
Excess reserves (percent of domestic currency deposits)	27.0	18.7	20.1	20.1	20.4	23.9	22.6	23.2	18.8
Multiplier of broad money supply	1.83	1.83	1.69	1.69	1.89	1.68	1.72	1.72	1.72
Multiplier of domestic currency supply	1.32	1.33	1.27	1.27	1.41	1.26	1.30	1.32	1.33

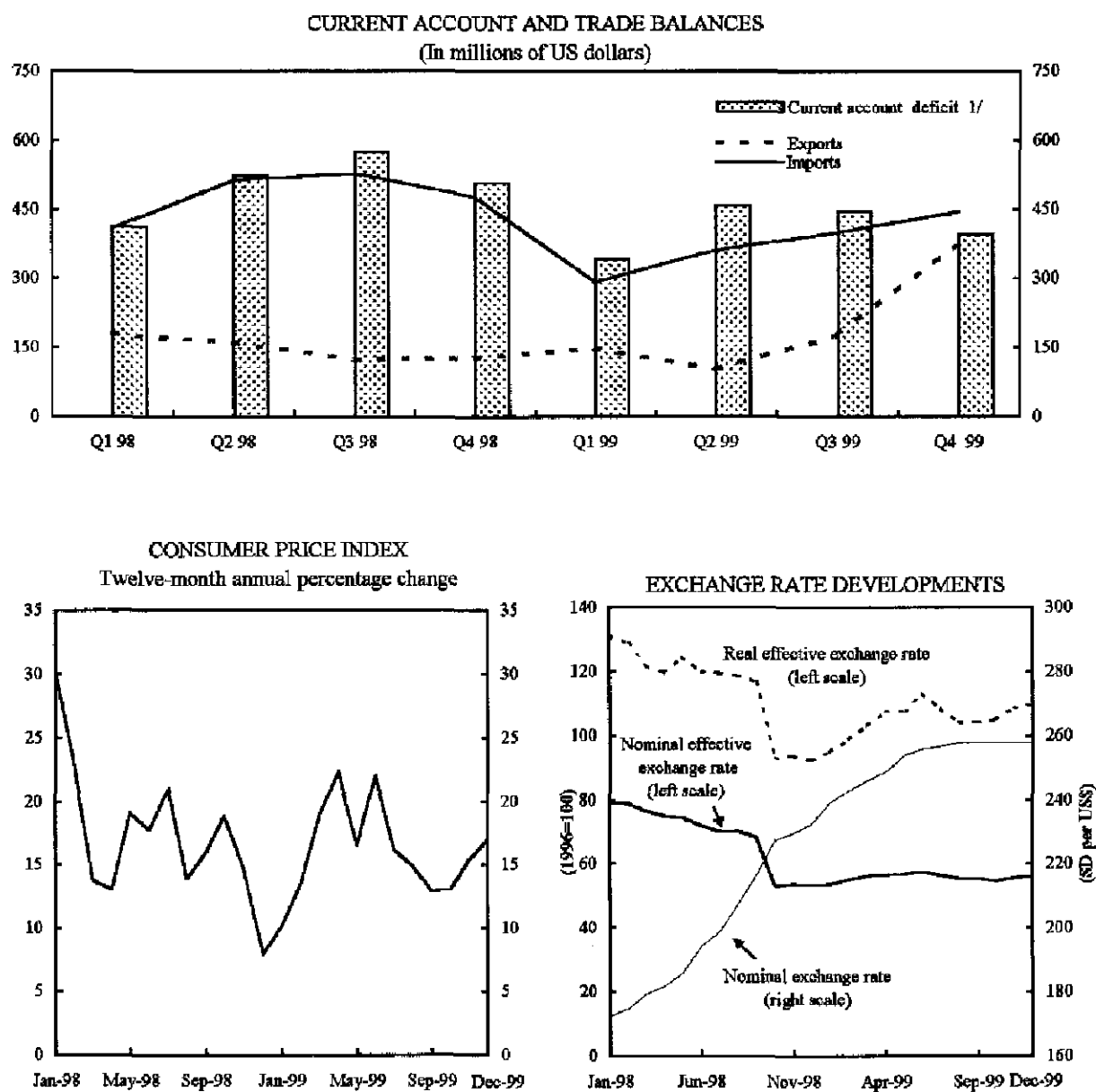
Sources: Sudanese authorities and Fund staff estimates.

1/ Revised due to reclassification at end-1999; see Table 4, footnote 1.

2/ The 2000 target for official reserve accumulation is subject to an adjustor; see Attachment, Table 1.

3/ Reclassified from reserve money in 2000.

CHART 4. SUDAN: EXTERNAL AND PRICE DEVELOPMENTS



Source: Sudanese authorities; and staff estimates.

1/ Excluding public transfers.

Table 6. Sudan: Summary Balance of Payments, 1997-2000

	1997	1998	1999		2000	
			Program	Est.	Program	Rev. Proj.
	(In millions of U.S. dollars)					
Trade balance	-985.5	-1,328.9	-820.0	-632.3	-113.9	56.5
Exports, f.o.b.	594.2	595.7	728.6	780.0	1,252.4	1,373.1
Cotton	105.6	95.6	52.1	44.9	72.9	52.1
Gum arabic	27.0	23.7	30.1	26.4	26.7	35.6
Livestock	78.3	120.3	127.4	114.3	117.2	123.9
Sesame	118.3	105.1	97.7	127.3	124.7	131.0
Oil	0.0	0.0	204.9	275.9	695.6	812.9
Other	265.0	251.2	216.4	191.2	215.2	217.6
Imports, c.i.f.	-1,579.7	-1,924.7	-1,548.3	-1,412.2	-1,366.3	-1,316.6
Foodstuffs	-237.9	-263.7	-288.0	-275.7	-322.3	-292.2
Petroleum	-292.7	-255.7	-274.7	-183.9	-99.3	-80.2
Other	-1,049.0	-1,405.3	-985.9	-952.6	-944.7	-944.1
Services (net)	-10.4	-27.3	-82.8	-87.6	-295.7	-286.0
Receipts	29.9	15.8	21.1	51.5	33.5	53.0
Payments	-40.4	-43.2	-103.9	-139.1	-329.2	-339.0
Of which: oil-related transport. expenses	0.0	0.0	-51.5	-85.2	-267.3	-282.4
Income (net)	-1,096.2	-1,147.2	-1,284.8	-1,291.8	-1,654.7	-1,714.3
Receipts	17.5	13.6	18.3	49.2	23.3	50.4
Payments	-1,113.6	-1,160.9	-1,211.0	-1,227.4	-1,309.9	-1,311.2
o/w: public interest payments due 1/	-1,108.4	-1,150.3	-1,204.6	-1,219.1	-1,294.5	-1,295.8
Oil related expenses	0.0	0.0	-92.0	-113.6	-368.1	-433.6
Current transfers (net)	451.6	507.1	534.9	456.8	562.8	503.8
Private transfers	428.9	490.2	504.9	445.8	533.4	501.0
Public transfers	22.7	16.9	30.0	11.0	29.4	2.8
Current account balance	-1,640.5	-1,996.4	-1,652.8	-1,554.9	-1,501.5	-1,440.0
Excluding public transfers	-1,663.2	-2,013.3	-1,682.8	-1,565.9	-1,530.9	-1,442.8
Capital account	4.1	0.0	0.0	22.7	0.0	13.0
Project aid	4.1	0.0	0.0	22.7	0.0	13.0
Financial Account (net)	-260.3	-141.7	-101.4	-61.2	-111.9	-100.3
Disbursements	18.6	13.0	40.0	42.4	39.3	39.3
Cash and commodity loans	0.0	0.0	0.0	0.0	0.0	0.0
Project loans	18.6	13.0	35.0	42.4	39.3	39.3
Amortization	-232.9	-219.3	-205.0	-206.5	-240.6	-240.6
Short-term capital flows (net) 2/	12.0	83.6	83.6	107.6	101.4	113.0
Commercial banks net reserve (increase -)	-58.0	-19.0	-20.0	-4.8	-12.0	-12.0
Errors & omissions and other private capital	619.9	840.8	434.8	272.8	313.7	339.5
FDI—Oil related	300.0	700.0	155.0	223.6	150.0	150.0
Other investments and E&Os	319.9	140.8	279.8	49.2	163.7	189.5
Overall balance	-1,276.8	-1,297.2	-1,319.3	-1,320.7	-1,299.7	-1,187.7
Change in official reserves (increase -)	-22.6	-25.4	-29.2	-36.2	-76.1	-188.5
IMF (net)	-23.4	-20.4	-9.2	-9.8	-31.1	-30.6
Change in arrears on repurchases	-57.5	-60.2	-40.0	-40.0	-60.0	-60.0
Change in arrears on charges	34.1	39.8	30.8	30.2	28.9	29.4
Other 3/	0.9	-5.0	-20.0	-26.4	-45.0	-157.9
Change in non-Fund arrears	1,299.3	1,322.6	1,348.5	1,356.9	1,375.5	1,376.2
Memorandum items:	(In percent of GDP)					
Current account deficit (incl. public transfers)	-19.9	-22.8	-17.5	-15.7	-14.7	-12.8
Excl. interest due and public transfers	-6.7	-9.9	-5.1	-3.5	-2.3	-1.3

Source: Staff estimates based on information provided by the Sudanese authorities.

1/ Includes estimates of late interest accrued during the year and Fund special charges.

2/ Net short-term trade and other credit facilities of the Bank of Sudan and commercial banks.

3/ The gross reserves accumulation target in 2000 is subject to an adjustor as described in the Attachment, Table 1.

accumulating US\$6 million of gross usable official reserves above program levels for a total US\$53 million.

11. **Relations with non-Fund creditors.** Through end-December, payments of US\$30 million were made to creditors other than the Fund, in line with the program benchmark. In the first months of 2000, Sudan cleared its arrears with the Arab Fund for Economic and Social Development (AFESD) and its full membership was restored. Discussions to regularize relations with the Kuwait Fund are underway. (Details in paragraphs 40–41.)

12. **The early economic indicators for 2000 are positive.** Both oil and non-oil revenue were strong in the first two months, and expenditure was below trend, allowing the government to build up deposits at the central bank. Inflation dropped in February from end-1999 peaks, although it remained unchanged in March in the low double digits. There has been no visible pressure on the exchange rate which has remained stable at around 257 dinars per U.S. dollar.

B. Implementation of end-December 1999 Structural Measures

13. **Previously delayed structural reforms moving forward** (Appendix III, Table 2). The June 1 starting date for the **introduction of the VAT** has been officially announced to the public, and the tax authority—under new management—has now completed basic staff training, and is vigorously pursuing public information programs and finalizing taxpayer registration. Implementing regulations for the **Investment Encouragement Act** have now been passed which go beyond previous expectations to close import tax loopholes by removing discretionary elements, such as by tightening the definition of goods to be exempted, limiting the number of exemptions, and providing exemptions uniformly to all investors, in addition to centralizing the exemption granting authority (paragraph 32).

14. **Remaining fiscal and monetary reforms for end-year completed.** The unified **taxpayer identification number** was introduced for large taxpayers as scheduled in December. Measures to reduce the size of **non-performing loans** and to ensure **adequate provisioning** were agreed between commercial banks and the BOS. The BOS has initiated its plan for coming to an agreement with non-compliant banks for achieving **appropriate capital adequacy ratios** (see paragraph 31 below). Finally, banks are now applying a **unified methodology for calculating incomes and profits** based on a 1998 BOS circular requesting that all banks adopt the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) accounting principles.

15. **The other structural benchmarks for end-1999 were completed as scheduled.** In the area of trade reform, the last remaining export tax—on cotton—was removed and the first phase of **import tariff reform** implemented, including the reduction of the maximum tariff to 60 percent and the number of tariff bands to 4, with a resulting average tariff of about 22 percent. The MTSMP's 1999–2000 **privatization plan** is on track: three enterprises are at the point of sale, and the government share in the telecommunications company (Sudatel) has

been decreased through the sale of shares to the public to 58 percent from 68 percent with a further reduction through an additional tranche slated to be sold through the stock exchange in the next month. Timetables for making **primary education compulsory** throughout Sudan have been adopted by the states: three states have already adopted compulsory primary education and the remainder have plans to introduce it by 2002.

IV. REPORT ON THE DISCUSSIONS

16. **Focus of the discussions.** With macroeconomic policy and outturn broadly in line with the program, the main issues during these discussions were sustaining and improving the current broadly positive macroeconomic conditions, implementation of the structural reform agenda without further delays, and the macroeconomic impact of the emerging oil sector. The first oil revenue accrued to the budget in the last quarter of 1999, and the authorities are only now beginning to grapple with the issues involved in being an oil producer—even if only a modest one—and are not yet fully confident that the projected levels of oil inflows will materialize (Box 2). The authorities were encouraged with the positive impact of past structural and economic reforms on the Sudanese economy and are eager to continue the reform program. However, they remained convinced that it would be most prudent to continue their steady but gradual approach to structural reform rather than risk political or economic disruptions by moving too quickly.

A. Medium-Term Macroeconomic Strategy

17. **Macroeconomic objectives.** The authorities agreed with the staff on the broad outlines of the medium-term macro framework, consistent with the MTSMP framework first set out in EBS/99/64, 4/28/99 and updated in the attached Memorandum of Economic Policies (Attachment, Annexes I and II). The objectives include real growth averaging 5.5 percent, inflation tapering off to 5 percent, and an improvement in the external current account and in the official reserve position—particularly following the anticipated increase in the government's share of oil production by 2004–05 (Table 7).

18. **Overall policy stance.** The economic objectives described above would require a macroeconomic policy mix that emphasizes fiscal discipline, combined with supportive monetary and flexible exchange rate policy throughout the medium-term period, with underlying structural reforms to improve resource allocation, encourage private sector investment, and ensure the non-oil sector is not neglected. The Sudanese authorities indicated their intention to pursue policies along these lines. Although growth may drop off in 2001 due to a decline in oil-related investment with the completion of the refinery and pipeline, it is expected to pick up gradually over the medium term as an increasingly open trade regime and market-friendly institutional environment encourage technology transfer and increased productivity. Higher total investment will need to be financed by increased domestic savings and private transfers, both spurred by a strengthening of the financial system. Inflation should be brought into the single digits through avoidance of further central bank financing and removal of structural rigidities in key sectors, such as agriculture. The removal of agricultural

Box 2. Sudan: Prospects for the Oil Sector Over the Medium-Term Horizon

Sudan exported its first oil in August 1999, some 40 years after the first attempts at oil exploration and two decades after oil exploration began in earnest in the southern part of the country. Based on completed exploration studies, proven reserves are estimated at 270 million barrels, which at current rates of extraction would last about five years. However, estimates of possible additional reserves in the Muglay basin raise the possible total reserves as high as 700–1,000 million barrels. Exploration, extraction and construction of a new pipeline and other needed infrastructure would put off any return from the unexplored regions for anywhere from five to fifteen years. In the meantime, oil revenue will fall off in 2001–03 as world oil prices (based on WEO projections) are expected to taper off. However, in 2004 government oil revenue will pick up sharply following the final cost recovery payment (which are paid in kind).

The onset of oil production provides an important boost to the economy. However, compared to other oil-producing countries, Sudan's discovered oil resources are small. The projections below are based on known reserves and indicate that as a share of total GDP, the oil sector is not expected to rise above 10 percent, assuming continued moderate growth in the non-oil sector. At the same time, relative to the monetized economy and as a share of total exports, oil revenue is quite large. Overall, the challenge to the authorities will be to design a medium-term oil policy which best harnesses the oil revenue inflows in the most productive manner while avoiding the dangers in mishandling oil revenue experienced by many other countries.

Oil Indicators

	1999	2000	2001	Projections			
				2002	2003	2004	2005
Oil Sector							
Crude oil production ('000 barrels/year)	14,885	32,800	66,000	75,900	75,900	75,900	75,900
Government share ('000 barrels/year):	5,992	22,049	27,562	31,696	31,696	54,648	54,648
Delivered to refineries	1,036	15,000	22,210	22,210	22,210	22,210	22,210
Crude exports	4,956	2,336	358	1,692	1,727	17,108	17,178
Pipeline fees	...	4,713	4,993	7,794	7,759	15,330	15,260
Oil export price equivalent (US\$/barrel) 1/	19.8	21.5	18.0	16.7	16.9	17.1	17.3
Oil sector/total GDP	0.6	4.0	4.4	4.8	5.3	5.8	6.4
Oil revenue/broad money	6.1	39.6	...	...	...	...	...
Fiscal Sector							
Oil revenue/GDP	0.6	3.3	3.2	3.0	2.8	4.3	4.0
Total revenue/GDP	8.5	11.5	12.1	12.1	12.2	14.0	14.0
Oil revenue/total revenue	7.6	28.4	26.5	24.3	22.7	30.6	28.7
External Sector							
Total crude oil exports (US\$ millions)	276	813	961	1,051	1,050	1,049	1,045
Government oil exports (US\$ millions)	65	48	6	27	28	280	284
Oil exports/total exports of goods and services	31.3	55.1	57.5	57.8	55.8	53.9	51.7
Government oil exports/total oil exports	23.7	6.0	0.6	2.6	2.7	26.7	27.2
Memorandum Item:							
Oil sector/GDP - Average OPEC country 2/	23.9	...	...	...	...	...	...

Sources: Sudanese authorities and Fund staff estimates.

1/ WEO consistent.

2/ 1994. The share of the oil sector in GDP was 48.4 percent in 1974 when many oil-producing countries first experienced large inflows of oil revenue.

Table 7. Sudan: Medium-Term Macroeconomic Scenario, 1998–2005

	1998	Est. 1999	Projection					
			2000	2001	2002	2003	2004	2005
(Change in percent)								
Production and prices								
Nominal GDP (SD billions)	1,986	2,443	2,914	3,346	3,775	4,180	4,636	5,153
Real GDP	5.0	6.0	6.5	5.3	5.4	5.5	5.7	5.9
Oil	0.0	13.1	8.4	6.8	6.8	6.6	6.8	6.9
Non-oil	5.0	6.0	6.4	5.3	5.4	5.4	5.6	5.8
Inflation (period average)	17.1	16.0	12.0	9.0	7.0	5.0	5.0	5.0
(In percent of GDP)								
Investment and saving								
Gross investment	17.6	16.7	17.4	16.3	16.0	16.3	17.3	18.4
Public sector	0.8	1.3	2.3	1.6	1.1	1.3	1.8	2.5
Private sector	16.8	15.4	15.1	14.7	14.9	15.0	15.5	15.9
Non-oil sector	10.6	12.3	12.3	12.3	12.6	12.8	13.5	13.9
Oil sector	6.2	3.1	2.8	2.4	2.3	2.2	2.0	2.0
Saving	7.7	13.2	16.1	15.8	15.8	16.2	17.6	18.8
Public sector	0.1	0.4	2.3	2.9	2.9	2.6	4.1	3.9
Private sector	7.6	12.8	13.8	12.9	12.9	13.5	13.5	14.9
External current account balance 1/	-9.9	-3.5	-1.3	-0.5	-0.3	-0.1	0.3	0.5
Central government operations								
Total revenue	7.9	8.5	11.5	12.1	12.1	12.2	14.0	14.0
Oil revenue	0.0	0.6	3.3	3.2	3.0	2.8	4.3	4.0
Non-oil revenue	7.9	7.8	8.3	8.9	9.2	9.5	9.7	10.0
Total expenditure	8.6	9.3	11.5	10.8	10.4	10.9	11.7	12.5
Current expenditures	7.8	8.0	9.2	9.2	9.3	9.6	9.9	10.1
Capital expenditure	0.8	1.3	2.3	1.6	1.1	1.3	1.8	2.5
Overall deficit (cash basis)	-0.7	-0.9	0.1	1.3	1.7	1.4	2.3	1.4
Foreign financing	0.2	0.3	0.7	0.3	0.3	0.2	0.3	0.3
Domestic financing	0.5	0.5	-0.8	-1.6	-2.0	-1.6	-2.5	-1.7
External sector								
External trade balance	-13.4	-6.4	0.5	2.1	2.4	1.9	1.4	1.0
Exports	6.0	7.9	12.3	13.0	13.2	12.7	12.1	11.7
Imports	-19.5	-14.3	-11.7	-10.9	-10.8	-10.7	-10.7	-10.7
Gross official reserves (months of imports)	0.2	0.5	2.0	3.0	3.3	3.4	3.7	3.9
Total external debt service (as percent of current receipts)								
Commitment basis	93.1	92.6	83.1	60.9	57.1	56.1	57.2	59.2
Actual payments	4.6	2.6	4.2	4.7	4.7	4.7	6.0	6.1
Terms of trade (change in percent) 2/	5.2	0.2	2.8	-0.6	0.8	1.2	1.2	1.4

Sources: Fund staff estimates and projections based on information provided by the Sudanese authorities.

1/ Excludes interest due and transfers; includes all oil transactions.

2/ Non-oil transactions.

taxes, investment in infrastructure and other agricultural reforms should drive non-oil export volume growth, while imports would stay above real GDP growth reflecting the import component of the government's capital spending and the tariff reform. Together with projected increases in oil exports, the resulting external adjustment should allow Sudan to further increase its gross reserves and debt service payments in the interest of pursuing its ongoing objective of normalizing financial relations with creditors.

19. **Medium-Term Fiscal Strategy.** The mission also discussed with the authorities the parameters of a medium-term fiscal policy, which should include saving the oil surplus either in financial assets abroad or in domestic productive investments with an identifiable stream of future returns—particularly those that would enhance competitiveness of the non-oil tradable sector. Attention was drawn to the need not to increase entitlements which may be difficult to sustain should there be a downturn in oil prices. The authorities were receptive to these ideas, although they emphasized the importance of investment in infrastructure relative to saving financial assets. It was agreed that the discussion on the medium term would continue in the next missions, particularly in the context of initial preparations for the 2001 budget. The mission also noted that any eventual resolution of Sudan's external debt problem would likely result in an increase in net repayments to external creditors.

B. Macroeconomic Policies for 2000

20. **Program for 2000.** For the remainder of 2000, the authorities intend to keep to a macroeconomic policy mix consistent with the program set out in February (EBS/00/22, 2/14/00), including moderate fiscal adjustment (depending on the outcome for oil revenue as discussed below), supported by a continuing cautious monetary policy stance. The objectives of real GDP growth of about 6.5 percent, a reduction in the inflation rate, a narrowing of the external current account and a further buildup in official reserves remain the same.

21. **Fiscal policy remains central to the macroeconomic policy strategy.** The budget targets an overall deficit of about 1 percent of GDP and limits central bank financing to 0.3 percent of GDP. However, the authorities reconfirmed their commitment to saving any oil revenue not needed to compensate for shortfalls in non-oil revenue and external financing; given currently high oil prices, it was acknowledged that the resulting adjustment could be significant in 2000. As noted, in the first two months of 2000 oil revenue was above budgeted levels. However, not yet confident of the expected oil windfall the authorities still remain concerned that **non-oil revenue** may fall short of projections due to possible under-collection during the initial stage of VAT implementation, the uncertain fiscal impact of trade reform, and the previous delays in reducing exemptions under the Investment Encouragement Act.

22. **Expenditure policy.** The staff encouraged the authorities to abide by the agreed **expenditure cap** and cut back expenditure should signs emerge that the program's inflation target would not be met. The government noted it fully intended to adhere to the expenditure cap; further, given the continued intensive needs for social and investment expenditure, any needed cuts would be made outside of allocations for these areas as possible. The mission also

reiterated concerns regarding the large increase in **military expenditure** in the 2000 program compared to the 1999 outturn—by 35 percent (against a 46 percent increase in total expenditure)—and encouraged the authorities to keep it below budgeted levels. In response, the authorities acknowledged the importance of keeping military spending in check in light of competing and more productive budgetary needs, and agreed to carefully monitor implementation of the allocation for military expenditure with a view to containing it as possible.

23. **Oil sector transparency.** In keeping with their commitment to transparency in **oil accounting** (Tables 8 and 9), the authorities provided the mission with oil sector data from the Customs Authority, the Bank of Sudan, and the Ministries of Finance and Energy; the resulting discrepancies found seemed to be due to start-up snags in the accounting procedures and have already been corrected. All government agencies involved in the energy sector, including the Ministry of Energy and the Sudan Petroleum Company, are subject to monitoring by the independent Auditing Department (see EBS/00/22). The staff finds the existing oil accounting policies broadly adequate, but mindful of possible emerging problems associated with oil production start-up and the authorities' relative inexperience, oil sector accounting will continue to be closely reviewed in the coming months.

24. **Domestic oil price increases.** The increasing divergence between domestic and international prices for petroleum products as world oil price continued to rise through early 2000 (and despite the increase in gas oil (by 25 percent) and gasoline prices (by 17 percent) in January) resulted in accumulated losses of the Sudan Petroleum Company (SPC) estimated by staff at about 17 billion dinars through end-March. These costs have been largely covered through transfers from the budget in 1999, a reduction in tax payments and profit transfers by the SPC, and access to SPC working capital. The agreed import-parity-based automatic **formula for pricing petroleum products** (gasoline, gas oil, and LPG) for domestic use was not triggered as expected on April 1. The extreme volatility in oil prices in the first three months of 2000 delayed the adjustment due to difficulties in determining the appropriate underlying FOB price. Since then, with the declines in world oil prices, domestic prices have moved back in line with world levels. With the start-up of petroleum products production at the Khartoum refinery, a new formula has been agreed for sales of crude oil by the central government to the Khartoum refinery (LOI paragraph 12). The central government will additionally desist from any further budget transfers to the SPC, shifting the burden to the SPC to adjust prices as needed. The mission urged the SPC to raise prices quickly to recover any remaining losses to its working capital. In addition, the mission noted that the move from import to export price parity has implications for overall government revenue in the absence of an appropriate adjustment in excise tax rates.

25. **Monetary policy stance to remain cautious.** Under the program projections, based on monetary growth in line with nominal GDP and a small decrease in velocity in keeping with the expected strengthening of the financial sector and continued stability of the exchange rate in 2000, limited recourse to BOS financing of the budget would allow official gross usable reserves to double to US\$98.4 million (still less than one month of imports) and credit to the

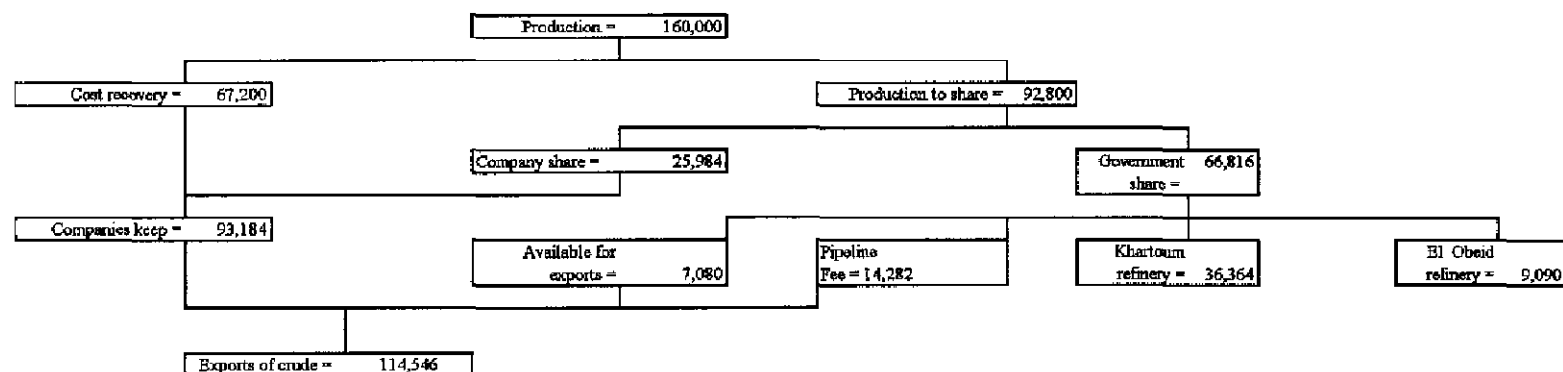
Table 8. Sudan: Government Revenue from Exports of Crude Oil, 2000

	2000
Production (1,000 barrels per day)	
Daily volume	160
Production days	330
Total volume (1,000 barrels per year)	52,800
Cost oil (1,000 barrels per year)	
Volume (42 percent of total production)	22,176
Profit oil (1,000 barrels per year)	
Volume (total volume less cost oil)	30,624
Government share (72 percent of total profit oil)	22,049
Investors' share	8,575
Government share of profit oil (1,000 barrels per year)	
Volume	22,049
Exports	2,336
Transportation fees in kind	4,713
El Obeid refinery	3,000
Daily volume (1,000 barrels per day)	10
Delivery days	300
Khartoum refinery	12,000
Daily volume (1,000 barrels per day)	50
Delivery days	240
Prices (US\$/barrel)	
Export price realized by government	20.75
UK Brent spot	24.50
Price adjustment	3.00
Export price FOB	21.50
Port fee Port of Sudan	0.75
Price realized by government at El Obeid Refinery	
Refinery gate	20.75
Price realized by government at Khartoum refinery	
Refinery gate	20.75
Revenue (US\$ millions)	
Government revenue from exports	48.5
Government revenue from El Obeid	62.3
Government revenue from Khartoum refinery	249.0
Total gross revenue (US\$ millions)	359.7
Repayment (US\$ millions)	68.0
Net government revenue(US\$ millions)	291.7

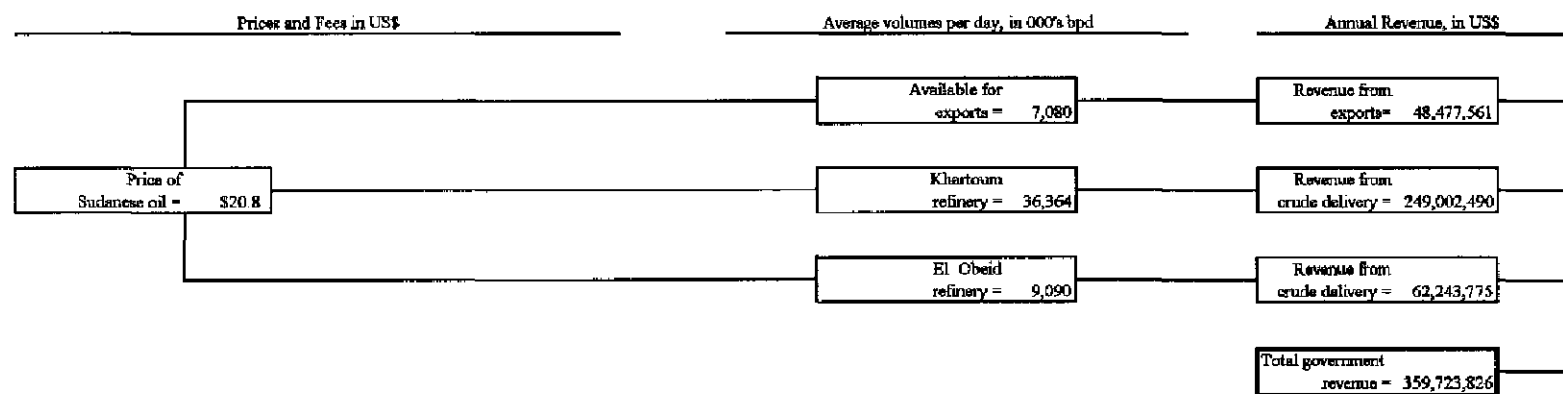
Sources: Data provided by the authorities and staff estimates.

Table 9. Sudan: Crude Oil Flows, 2000

1. Flows of domestically produced crude: Daily average for whole of 2000 1/
(in barrels per day)



2. Revenues to the budget, 2000



3. Calculation of BOP flows, 2000

Exports of crude oil		Oil-related transportation expenses		Oil-related income expenses	
Volume of crude, bpd =	114,546	a. Transportation of non-gov't oil destined for exports		a. Cost recovery, bpd	67,200
Days of production =	330	volume =	93,184	b. Companies' share, bpd	25,984
Export price, FOB =	\$21.5	days =	330	Price adjusted for transportation costs and fees at Port Sudan	\$14.75
Total value (US\$ million) =	812.7	fee =	6.0		
		cost =	184.5	Total income expenses, (US\$ million) =	453.6
		b. Value of crude received as payment in kind			
		volume =	14,282		
		days =	330		
		export price =	20.8		
		cost =	97.8		
		Total (US\$ million)	\$282.3		

Source: Data provided by the Sudanese authorities and Fund staff estimates.

1/It is assumed that operations (production, exports, processing) take place for 330 days.

private sector to increase by 27 percent in real terms. Given current expectations for world oil price trends, a significant additional increase in reserve accumulation would be expected. However, the Central Bank Governor voiced some concern in this area, noting that in exceptional circumstances of heavy pressure on the dinar, a full adjustment on reserve accumulation might not always be possible. While noting the Governor's concerns, the mission observed that using any windfall receipts from larger than expected oil exports to build up reserves would be consistent with allowing more flexibility in the market determined exchange rate (see paragraph 27). Finally, the authorities assured the staff of their commitment to remaining vigilant to the possible reemergence of inflationary pressures and to tighten demand management as needed.

26. **Sharp decline in credit to the private sector.** The staff raised concerns regarding the lack of private sector credit needed to finance economic growth (Box 3). The BOS shared these concerns, observing that the liberalization of the financial system that has taken place to date—including the removal of directed credits—has effectively revealed underlying weaknesses in the banking sector. The authorities acknowledged that continuing structural problems were discouraging the extension of credit, such as laws which made loan collection difficult, and outlined a program to reduce the cost and increase the availability of credit to the private sector (paragraph 31 below).

27. **Exchange rate policy.** The authorities believe the current stability in the exchange rate reflects current market demand and supply (the exchange rate has remained virtually unchanged at 257 dinars to one US dollar since October 1999). The mission repeated its concerns that excessive stability in a situation where inflation remained at the 10–15 percent level could lead the market to perceive the BOS as endorsing the current exchange rate—which in fact could not be supported through intervention if heavily challenged or if faced with a balance of payments shock given the current low levels of reserves. Anecdotal evidence suggested that the exchange rate is already widely considered fixed within both the public and private sectors. The mission also expressed concern about the medium-term impact on external competitiveness of traditional exports, particularly given the perceptible tolerance for a moderate level of inflation. In response, the BOS recalled its assessment that the current stability was in line with the improvement of the economic environment and the return of business confidence, and pointed to their initial conclusions that the real appreciation experienced to date had not had any visible adverse impact on the competitiveness of the traditional export sectors. The mission observed that, while commercial banks are free to transact among themselves, they prefer to trade directly with the central bank given the narrow intervention band and the absence of counterparty risk. The BOS noted it has taken steps to deepen the foreign exchange market, most recently by removing in February the seven-day limit on commercial banks holding foreign exchange and increasing the spread between its buy and sell rates to 1 dinar, and that additional steps are planned for the near future (paragraph 31 and Box 4). As in other areas of the reform program, the BOS strategy is to maintain a steady but gradual pace of reform to avoid destabilizing the market.

Box 3. Sudan: Decline in Credit to the Private Sector

Credit to the private sector dropped sharply in both nominal and real terms in 1999; particularly affected were the agricultural, industrial, and construction sectors. Credit for domestic trade continues to be subject to a ceiling imposed by the Bank of Sudan.

Credit to the Private Sector, 1997-99

	December		
	1997	1998	1999
(End of period; in percent unless indicated otherwise)			
Credit to private sector (SD billions)	39.4	44.3	43.6
Growth rate	23.3	12.7	-1.7
Inflation rate	32.0	7.9	17.0
Real growth rate	-8.7	4.8	-18.7

Source: Bank of Sudan

To some extent, the decline in credit was expected and could be considered healthy. In the past directed credits (discontinued in early 1997) pushed up the level of nonperforming loans. Thus, lower credit growth could be seen as a sign of better risk assessment and improved vigilance by commercial banks and a more efficient allocation of financial resources. From 1999, it also reflects the BOS' cautious prudential policy which now looks more closely at the quality of banks' loan portfolios. However, the sharpness of the decline in 1999 alone raises some alarm, given the need for the banking system to finance private sector growth.

Among other reasons for the decline in credit to the private sector to be considered are the following:

- * The capital and deposit base of most banks is narrow, eroded by high inflation of past years. Many banks are undercapitalized and do not yet comply with the 8 percent capital adequacy ratio.
- * Banks are reluctant to extend credit to agriculture because, in the past, 85 percent of these loans have been unrecoverable.
- * The cost of borrowing, while declining, remains high. At end-March 2000, the average Murabaha lending rate stood at 26 percent (10 percent in real terms) and ranged as high as 34 percent (17 percent in real terms).
- * Rigidities imposed by some Islamic modes of financing add structural constraints to lending operations.
- * Most banks have no lines of credit extended from abroad.
- * Existing legislation creates significant difficulties in collecting loan repayments.

Box 4. Foreign Exchange Market Reform Agenda: 1999–2000

1. The step-by-step regulatory reform of the foreign exchange system by the Bank of Sudan (BOS) that culminated in the unification of the foreign exchange market in late 1998, was followed by significant reform measures in 1999 that deepened the foreign exchange market, increased its transparency, and removed a number of restrictions. The 2000 agenda seeks to consolidate the recently achieved gains by further liberalizing the exchange rate regime, including through deepening the still nascent interbank foreign exchange market.

1999 Reforms Completed

2. **Encouragement of interbank market.** Early in the year, with surrender requirements on a range of products and services still in place, the BOS established an auction system to distribute foreign exchange to the market. In parallel, it encouraged commercial banks to develop dealing rooms. Once active dealing rooms were established, the BOS discontinued the auction system. As a result, an interbank market, although still thin, has emerged.

3. **Regulations eased and surrender requirements eliminated.** The 2-day limit for the banks to sell unused foreign exchange was extended to 7-days, and the limit for exporters to repatriate their export earnings was increased initially to 45 days and later to 60 days. Exporters have an additional 20-days to convert unused foreign exchange to dinars. The BOS also eliminated all remaining surrender requirements related to the export of goods (on cotton and gum arabic). In addition, all export taxes and the stamping requirement were also abolished.

4. **Updated regulations introduced.** New foreign exchange regulations and a code of conduct were adopted. Since the exchange rate was unified, the daily exchange rate is determined in the market, and the official accounting rate set as the median commercial bank rate of the previous day.

5. **Range of market participants expanded and confidence in the system improves.** As a result of these reforms, commercial banks have emerged as the most dynamic non-BOS participants. Nonbank dealers have lost their significance as market participants increasingly find it more convenient to deal directly with banks. To encourage dealers to continue to play a role in the market (in part to provide competition to the banks) the BOS eliminated the \$50,000 maximum limit per transaction to free the range of activities they can undertake. The increasing availability of foreign exchange has helped stabilize the foreign exchange rate and the long queues for foreign exchange have disappeared. However, through end-1999 the BOS continued to be actively involved in the market and to deal with commercial banks on demand.

2000 Reform Agenda

6. **The BOS's strategy for 2000 is to gradually minimize its role in the interbank market.** While commercial banks are free to transact among themselves, they prefer to trade directly with the central bank given the narrow intervention band and the absence of counterparty risk. The BOS has agreed to not always stand ready to buy or sell and to take further steps to encourage interbank market transactions; however, it has also reaffirmed its intention to continue its strategy of a steady but gradual pace of reform of the foreign exchange market.

7. **Further liberalization.** In line with these objectives, in early 2000 the BOS has: abolished the 7-day limit on banks to sell unused foreign exchange to the BOS, widened the spread between its buy and sell rates to one dinar (0.3 percent), and ended the mandatory transfer of remittances from Sudanese working abroad to the BOS. Additional steps planned for 2000 include:

- Further widen the buy and sell spread to 0.5 percent in June.
- Phase out the remaining surrender requirement on oil sector services to further encourage bank intermediation and increase the flow of foreign exchange through the market.
- Improve the clearing system to ease banks' concerns that counterparties will not settle on a timely basis the local currency part of the transaction.
- Eliminate all limits on exporters' holdings of foreign exchange.

28. **Export competitiveness.** An initial assessment prepared by the staff concludes that the profitability of some traditional crops has declined in 1999 reflecting lower productivity in the irrigated sector, declines in crop yields due to the deterioration of infrastructure in the irrigated sector, as well as the recent real exchange rate appreciation. However, most crops remain competitive and prices do not appear to be the major constraint on exports, according to merchants, and the expected increases in productivity in the irrigated sector in 2000 could reverse the previous year's losses in competitiveness. A detailed Ministry of Finance study on competitiveness should be completed by end-September 2000, with preliminary recommendations ready in May. In the meantime, measures are already underway to reduce structural rigidities in the main agriculture export sector through the reduction of state agricultural taxes and the removal of ad-hoc interstate trade taxes, and investment in agricultural infrastructure that should improve productivity and export competitiveness.

C. Structural Reform Policies

29. **Fiscal sector reforms broadly on track.** The authorities are focused on introducing the VAT by June 1 and minimizing the anticipated transitional difficulties in the early stages of implementation. They are fully aware of the need to improve the generation of non-oil revenue—despite the new inflows of oil revenue—in particular given the low levels of non-oil revenue as a percent of GDP compared with international standards, possible revenue declines from future customs tariff reductions under the trade reform program, still limited projections of oil reserves, and the need for a safeguard against unexpected downturns in oil prices. This would need to be achieved through further improvements in tax administration. Regarding **public expenditure management**, the budget accounting office has submitted to the Council of Ministers a study on the requirements for the introduction of full GFS classification of revenue, expenditure and financing along with a proposal for bringing forward the timing for GFS reclassification of the government accounts to end-2000. Technical assistance from the Fund on expenditure management is expected in May 2000.

30. **Monetary policy instruments.** In the discussions with the authorities on monetary policy and financial sector issues, the mission noted the challenges faced by the authorities in conducting monetary and financial policy within the framework of an Islamic financial system. To further expand the range of monetary policy instruments, the authorities plan to build on the successful introduction of the GMC through measures to develop the interbank market (LOI paragraph 18) and to convert an additional tranche of government debt stock held at the BOS into GMCs. Competitive credit auctions to banks have begun. The BOS has developed a plan for further gradual liberalization of the financial system through end-2000, which will include narrowing the gap between reserve requirements on domestic and foreign currency deposits, lowering the overall reserve requirement level, and easing the credit ceiling on trade.

31. **Bank soundness important for medium-term macroeconomic objectives.** The authorities recognize the existing weaknesses in the banking system. Nonperforming loans remain high at 18 percent of total loans, and the BOS has classified 10 of the 26 commercial banks operating in Sudan as undercapitalized, with capital adequacy ratios below 8 percent.

The BOS and commercial banks have agreed on measures to reduce the size of non-performing loans and strengthen provisioning, and discussions are underway between the BOS and banks to ensure compliance with new minimum paid-in capital and capital adequacy requirements (LOI paragraph 19). The BOS expects that considerable voluntary bank restructuring will take place as these measures are implemented, and banks are expected to merge or be liquidated if not able to raise the required additional capital. Two undercapitalized banks have already been liquidated. The Fund will be providing technical assistance to the BOS on bank restructuring, as well as for improving banking supervision. To increase the availability of credit to the private sector, the BOS will also take other steps, including development of alternative Islamic instruments to improve the availability of agricultural financing, amending laws which are seen to have undermined banks' ability to collect overdue loans, ceasing to endorse the setting of minimum commissions and fees by commercial banks, and devising a system of market-based incentives to strengthen the deposit base of banks.

32. **External sector reforms move forward as well.** The new implementing regulations for the Investment Encouragement Act have become effective, considerably streamlining the exemptions on import tariffs available to investors and giving a committee chaired by the Ministry of Industry and Investment sole responsibility for determining eligibility for such exemptions (LOI paragraph 20). All the new exemptions and customs tariff rates will apply uniformly to all investors importing these products. The Ministry of Finance estimates the net impact on the budget of these reforms should be positive. The trade reform agenda for the remainder of 2000 includes reform of the role of export councils and elimination of the list of essential goods which can be imported using bank credit facilities. To further deepen the foreign exchange market, the BOS plans to widen the spread between its buy and sell rates to 0.5 percent by June 2000 and eliminate limits on exporters' holdings of foreign exchange by December 2000. Future steps to further encourage the interbank foreign exchange market include improvements in the clearing system to ensure that counterparties settle transactions on time.

33. **Exchange restrictions.** Sudan maintains one inoperative bilateral payments agreement with a Fund member subject to approval under Article VIII, Sections 2 (a) and 3. The staff encouraged the authorities to eliminate this restriction. The authorities indicated that all of Sudan's external payments arrears arise from government or publicly-guaranteed debt of entities that are part of the budgetary process. Thus, they do not give rise to exchange restrictions.

34. **In the key agricultural sector, several reforms are underway.** A pilot reform program for selected sections of the Gezira irrigation scheme formulated by the FAO and the World Bank is about to begin, including allowing farmers greater freedom in crop rotation and water management. In addition, the Government recently announced that farmers are no longer required to produce cotton (the remaining compulsory crop). More broadly, steps have been taken to reduce the overall tax burden on agricultural products and trade (LOI paragraph 23).

35. **Measures to encourage private sector investment.** In the electricity sector measures are underway to provide an efficient and stable power supply, including further retrenchment, cuts in consumer subsidies and revision of the tariff structure, and encouragement of private investment in the sector (LOI paragraph 24). While the private sector appeared to regard the **regulatory framework** in Sudan as broadly satisfactory following recent reforms, **judicial reform is needed**—particularly in updating obsolete legislation as noted above (LOI paragraph 25).

36. **Social policies are a priority for Sudan.** The government's social policies continue to aim at improving Sudan's very weak social indicators, in particular by introducing universal basic education and extending primary health care to the entire population. In line with these goals, priority is given in the 2000 budget to social and development spending, including through higher transfers to the states for this purpose. Proposals are under consideration for improving the monitoring and control of transfers to the state to ensure that transferred funds are used for the designated purposes. Three states, including Khartoum State, now have introduced compulsory primary education. Work with the World Bank continues on four studies covering poverty, social services (water, education and health) displaced people, and vulnerable groups that are expected to be completed in 2001. The social sector studies would provide a basis for the Government to initiate necessary actions, including shifting spending priorities and policies as well as mobilizing resources, to improve access to identified social services. In the meantime, following participation in a regional IMF/World Bank seminar on poverty reduction, the government has now begun formulating its own poverty reduction strategy.

D. Other issues

Data and technical assistance issues

37. **The available statistical data are sufficient for program monitoring, however statistical weaknesses continue to hamper economic analysis.** These deficiencies include long lags in the compilation of national accounts, incomplete fiscal data on state budgets, and the misclassification of several monetary accounts, which necessitates frequent reclassification of the accounts (such as that for other items net).

38. **Improvements in the statistical base is an important objective under the MTSMP.** Passage of the Statistical Act, expected in mid-2000, should strengthen the institutional capacity of the Central Bureau of Statistics (CBS) and allow it to begin introduction of the 1993 System of National Accounts (SNA) (LOI paragraph 26). The BOS plans to improve classification problems in its balance sheet and in the consolidated balance sheets of commercial banks, with IMF technical assistance expected in May, and in cooperation with commercial banks and certified accountants (a full discussion of data issues can be found at Appendix I, Annex I). Further improvements in the BOS' collection of balance of payments data are also underway. Finally, in line with its commitment to improve

transparency and responding to the growing private sector interest in data, the BOS plans to launch an Internet web site with key economic and financial indicators and policy documents.

39. Sudan has a broad need for technical assistance in implementation of the government's macroeconomic and structural reform program. The Fund will be meeting that need to a considerable extent, particularly in the areas of fiscal and banking reform, as well as on statistical issues. However, currently very little technical assistance is available from other donors.

Relations with Creditors

40. **Payments to the Fund.** The authorities have reaffirmed their commitment and returned payments to the Fund to US\$60 million in 2000. Still uncertain about projected levels of oil revenue inflows, the authorities expressed concern regarding the overall increase in debt service payments now needed in 2000. However, if warranted by balance of payments developments, the authorities agreed to consider increasing payments to the Fund above specified levels later in 2000, with a view to further facilitating the de-escalation process. Regarding payments to other external creditors, the authorities have agreed to resume payments to the World Bank at the level previously agreed for the year after temporarily suspending payments while assessing overall obligations in 2000. Given these and other commitments, the authorities now project total payments to creditors to be about US\$120 million in 2000. The staff encouraged the authorities to continue its efforts, which have met with reasonable success to date, in re-establishing relations with external creditors, which will be an important ingredient in moving toward eventual resolution of Sudan's external debt.

41. **Progress continues in normalizing relations with external creditors.** By end-1999, Sudan had normalized relations with the Saudi Fund for Development, Abu Dhabi Fund, and OPEC Fund, and continued to maintain good relations with IFAD and IDB. In early 2000, Sudan reached an agreement with the Arab Fund for Economic and Social Development (AFESD) that allowed it to clear US\$200 million in arrears through offsets against government spending on several projects completed after 1992. In April, the AFESD Board of Governors voted to restore Sudan's full membership. More recently, discussions have begun with the Kuwait Fund on an agreement that would lead to the clearance of Sudan's arrears and the regularization of their financial relations.

Program monitoring issues

42. In December 1999, to address a recurrent accounting problem, the BOS reclassified as claims on the central government all outstanding claims on the central government from the past three decades previously included in suspense accounts and classified under **other items net**. The resulting reclassification causes a break in the monetary aggregates series.³

³Examples of these claims were the costs of printing currency and losses of public corporations assumed by the BOS.

43. In consultation with the World Bank, the December structural benchmark for the Government to agree with the World Bank on actions plans for alleviating poverty and social service delivery will be deferred until a later date. A full reassessment of all structural benchmarks for the second half of 2000 will take place during the first review of the Second Annual Program under the MTSMP.

V. STAFF APPRAISAL

44. Following years of economic decline, over the last three years under staff-monitored programs, Sudan has made considerable progress in stabilizing the macroeconomic situation and moving forward the structural reform agenda. That this progress has been attained against the background of several natural disasters, a civil conflict, and very limited international financial support is testimony to the authorities' strong ownership of the overall adjustment and reform program. Macroeconomic policy now appears roughly on track with the basic macroeconomic objectives of moderate growth and lower inflation achieved. There are also continuing signs that private sector confidence is improving, including the success of the first GMC tranche, the stability in the exchange rate, and a downward trend in the share of foreign currency deposits in broad money. Against this background, the authorities' priorities will need to be consolidating and sustaining the improvement in the macroeconomic situation and pushing forward the structural adjustment program. The new policy issue to consider in the immediate future and over a longer horizon is avoiding mismanagement and making the best use of the new oil resources.

45. The macroeconomic objectives of the 1999 SMP were broadly achieved, although as expected the overall macroeconomic situation was modestly more expansionary than programmed. Central bank financing of the fiscal deficit and inflation were both somewhat above program, and while targets for growth of broad money and net domestic credit were broadly met, the increase in reserve money was significantly above projections, possibly due to stronger than expected seasonal demand for currency. Although the inflation rate was brought down, it remains moderately high in the low double digits. Early data indicate that the 2000 program is on track, with a reduction in the government's net position at the central bank through February and the likelihood, if oil prices remain strong, of a further substantial improvement by end-year. The implementing regulations reforming the Investment Encouragement Act have been passed, and preparations are on track for the June introduction of the VAT. Finally, the staff welcomes the authorities' successful efforts to date to improve relations with external creditors.

46. For 2000, Sudan has adopted and is following a broadly appropriate package of structural reforms and macroeconomic program, although somewhat more ambitious targets for reducing government borrowing and inflation, and a more modest increase in government expenditure, would have been welcome. Moreover, considerable risks to implementation of the overall program remain. Public expectations and political pressures for use of oil revenues are rising and could result in excessive increases in government spending, the erosion of non-oil revenues, and the deterioration of the external competitiveness of the non-oil sector, as has happened in many low-income oil producers. Moreover, the expected oil revenue, while

providing a welcome boost to the fiscal accounts, will not on its own be sufficient to cover required increases in development and social spending. Further, while the financial authorities recognize the need and have committed to limit military spending as possible in light of competing budgetary needs, pressures for increased expenditure in this area are not likely to abate in the near future. Finally, structural weaknesses in the economy, including deteriorating infrastructure in the agricultural sector, low investment in physical and human capital, scarcity of external assistance, an unsustainable debt burden, and weak banking system intermediation, continue to pose challenges for the policy makers.

47. The focus of the 2000 macroeconomic program will continue to be further modest consolidation of the fiscal accounts supported by a cautious monetary policy stance, particularly in light of continued high levels of inflation. As the staff believes the program could have been somewhat tighter, the authorities are encouraged to remain vigilant to the possible resurgence of inflationary pressures and to cut back expenditure as needed, particularly military expenditure. Regarding the exchange rate, while noting that the continued stability has some basis in the improved macroeconomic situation and private sector confidence, and that no pressures on the exchange rate nor major damage to overall competitiveness have emerged, the staff urges the authorities to move rapidly to develop the interbank market through further liberalization to allow room for increased flexibility and a further reduction in the BOS' role in the market.

48. Regarding strengthening of the financial sector, the staff fully shares the authorities' concerns regarding the decline in credit to the private sector. The BOS is urged to move quickly to implement the planned steps, in particular those involving updating of laws and other reforms of the judicial sector which would remove impediments to the extension of credit and taking the necessary steps to deepen the interbank money market. Turning to the plans to address weaknesses in the banking sector, the staff recognizes that this will be a large and complicated undertaking and supports the BOS' objectives in restructuring the banking system.

49. As a whole, the structural reform agenda is moving forward. The end-1999 benchmarks have been met or are expected to be completed shortly and the efforts made in these areas are welcome. However, for the future the authorities are urged to keep to schedules and avoid further delays in the structural reform agenda, particularly those measures key to ensuring the continuing competitiveness of the non-oil traded goods sector. The staff strongly urges the authorities to ensure that petroleum product prices are adjusted without further delay to recoup remaining losses and for the future to allow the system to operate so as to fully and automatically reflect changes in world market prices, thus finally removing government decision-making from this politically sensitive issue. The staff additionally notes with disappointment that the petroleum pricing mechanism is based on export rather than import parity which will have implications for overall government revenue. The recent liberalization of cotton cultivation shows that, while important strides in structural reforms have been made across all sectors of the economy, there remain pockets of government regulation which remain to be addressed.

50. The staff welcomes the authorities' commitment to **transparency in oil accounting**, as evidenced by the provision of oil revenue data and other oil sector information from the relevant government agencies. Some initial discrepancies found are now corrected and seemed to be due to start-up snags in the accounting procedures. Given the importance of maintaining accurate accounting in this sector, the staff strongly encourages the authorities to ensure that earlier discrepancies do not re-emerge and to maintain the current transparent accounting procedures.

51. Regarding **provision of data** to the Fund for conducting surveillance, while the available data are sufficient for program monitoring, statistical weaknesses continue to hamper economic analysis in several areas, including delays in national accounts compilation and particularly recently emerged weaknesses in the monetary data. The authorities are aware of these deficiencies and an improvement in the statistical base is an important objective under the MTSMP.

52. Looking ahead, a key objective will be finalizing discussions regarding **best practices for use of oil revenue** over the medium term. The staff encourages the authorities to save the oil surplus either in financial assets abroad or in domestic productive investments with an identifiable stream of future costs and returns. Additionally, the authorities should not be distracted from improving revenue administration over the medium term, given the low levels of non-oil revenue and as a safeguard against unexpected downturns in oil prices.

53. Given the continued weak social indicators, the staff is encouraged by the authorities' focus on increasing social and development expenditure and particularly welcomes the efforts to begin framing its own poverty reduction strategy.

54. The staff continues to believe that Sudan has adopted a broadly appropriate macroeconomic framework and package of structural reforms for 2000 and that performance to date under the MTSMP has been satisfactory. For the immediate future, it will be important for the authorities to maintain the current momentum in successfully implementing the overall program, particularly in light of expected decision points in the near future. Thus, the authorities are urged to guard against the temptations possibly brought about by the new oil revenue inflows and to not relax their policy stance. Rather, they are urged to sustain and build on past positive economic performance, preserving and improving the broad macroeconomic stability achieved to date, and to carry forward the structural reform program. In addition, they are encouraged to continue their efforts to improve relations with external creditors as essential for an eventual resolution of the external debt problem.

55. With the unification of the exchange market in October 1998, the only restriction subject to Fund approval under Article VIII arises from the outstanding balance under an inoperative bilateral payments agreement with Egypt. In the absence of a definite timetable for the settlement of the outstanding balance under this agreement, the staff does not recommend approval of this restriction.

56. It is proposed that the next Article IV consultation with Sudan take place on the standard 12-month cycle.

Sudan: Fund Relations

As of March 31, 2000

I. **Membership Status:** Joined 9/05/57; Article XIV

II. General Resources Account:	<u>SDR Million</u>	<u>% Quota</u>
Quota	169.70	100.0
Fund holdings of currency	620.60	365.7
Reserve position in Fund	0.01	0.0
III. SDR Department:	<u>SDR Million</u>	<u>% Allocation</u>
Net cumulative allocation	52.19	100.0
IV. Outstanding Purchases and Loans:	<u>SDR Million</u>	<u>% Quota</u>
Stand-by arrangements	240.77	141.9
Extended arrangements	164.57	97.0
Contingency and Compensatory	43.05	25.4
Trust Fund	59.23	34.9
First Credit Tranche	2.48	1.5

V. **Financial Arrangements:**

<u>Type</u>	<u>Approval Date</u>	<u>Expiration Date</u>	<u>Amount Approved (SDR million)</u>	<u>Amount Drawn (SDR million)</u>
Stand-by	06/25/84	06/24/85	90.00	20.00
Stand-by	02/23/83	03/09/84	170.00	170.00
Stand-by	02/22/82	02/21/83	198.00	70.00

VI. **Projected Obligations to the Fund:**¹ (SDR million; based on existing use of resources and present holdings of SDRs);

	<u>Overdue 03/31/2000</u>	<u>Forthcoming</u>				
		<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
Principal	510.1	--	--	--	--	--
Charges/Interest	<u>616.4</u>	<u>18.8</u>	<u>25.1</u>	<u>25.1</u>	<u>25.1</u>	<u>25.1</u>
Total	1,126.5	18.8	25.1	25.1	25.1	25.1

¹The projection of charges and interest assumes that overdue principal at the report date (if any) will remain outstanding, but forthcoming obligations will be settled on time.

Nonfinancial Relations

VII. Exchange and Trade Arrangements

Sudan has an independently floating exchange rate. The legal tender is the Sudanese dinar, which replaced the Sudanese pound in proportion SDI=LSd 10 in 1999. Since October 1998, the exchange rate system has been unified—market participants determine the exchange rate and trade freely within a unified regulatory framework. The Bank of Sudan (BOS) administers the exchange control and actively transacts in the foreign exchange market at negotiated rates. For the purposes of accounting for official transactions, the BOS calculates the official exchange rate as the median rate quoted by commercial banks the previous day. This rate is regularly published by the BOS and is used mainly for customs and budgetary transactions.

The trade regime in Sudan has been gradually liberalized. With a few minor exceptions for religious and security reasons, all exports are free from nontariff restriction. With the same exceptions, all imports are free from nontariff restriction. Sudan uses four import tariff bands, with the average import tariff of 22 percent. The only surrender requirements still in effect are: the 20-day limit on exporter's holdings of foreign exchange; and the surrender of proceeds from payments related to services in the petroleum sector. Sudan maintains one inoperative bilateral payments agreement with Egypt.

VIII. Article IV Consultation

The last Article IV consultation discussions were held during March 2–18, 1999. The Staff Report (EBS/99/64, 04/28/99) and the RED (SM/99/96, 04/28/99) were discussed by the Executive Board on May 12, 1999.

IX. Technical Assistance

In January 1995, the Executive Board decided to resume Fund selective technical assistance (TA) to Sudan. Since then, there have been the following TA missions: (i) reform of indirect taxation (August 1995, March 1997, May 1997, October 1997, May, October, November 1998, and October 1999); (ii) multisector technical assistance in statistics (September/October 1995); (iii) exchange system reform (April 1997, November 1997, May and September 1998); (iv) monetary management and banking supervision (June 1997, November 1997, May, September, December 1998, May and October 1999); (v) government finance statistics (June 1997 and May 1998); (vi) monetary statistics (July 1997 and May 2000); (vii) balance of payments and monetary statistics (April 1999); (viii) expenditure control and management (September 1997, May 1998, and May 2000); (ix) oil sector taxation (October 1999); and (x) training course on financial programming and policies (April 2000). Since October 1999, a long-term TA expert has been assisting the authorities with the preparation for the VAT.

X. Resident Representative

The Fund's resident representative in Khartoum was withdrawn in June 1990.

Sudan: Data Quality

Type of data	Scope and timeliness of reporting	Adequacy for monitoring	Areas of concern	Steps to improve integrity
Real sector National accounts	Historical data reported on time by CSO	Broadly acceptable: real and nominal GDP by sector available with a 2-year lag	1968 SNA still in use; oil sector value-added calculation not completed; no real GDP by expenditure; 4-year delay in nominal GDP by expenditure; private consumption derived as a residual; estimations rather than surveys are used for some GDP components	Rebuild the CBS institutional capacity; introduce of 1993 SNA; conduct census of agriculture production. Implement in full the multisectoral 1995 TA mission recommendations.
	Last and current year estimates reported to missions by MOF	Acceptable	Estimates are based on incomplete data, in particular for oil value-added, livestock, and fruit and vegetable production.	Better coordination between MOF, CBS, and Ministry of Agriculture needed.
Prices	Monthly CPI reported on time, with a minimal lag	Acceptable: only CPI for Khartoum area available promptly; weekly CPI upon request	CPI for Sudan as a whole available with a 4-month lag and its coverage still incomplete; the CPI is based on an outdated consumer basket; income-group indices are not regularly aggregated into CPI.	Conduct new household income and expenditure survey; reduce timing discrepancies and other reporting inefficiencies by individual states.
	Monthly WPI reported on time, with a minimal lag	Acceptable	Weighting scheme is not available; WPI based on prices for 32 mainly agricultural commodities.	Introduce WPI methodology consistent with SNA.
Government Finance	Monthly reporting of main budgetary items, generally on time; 1.5-month lag	Good: main revenue and expenditure items reported, financing consistent with monetary accounts	No complete data on state budgets available; incomplete functional classification; MoF allocations to ministries are reported, but not their actual expenditure; slow progress on the introduction of the GFS classification.	Introduce the GFS classification; improve accounting and reporting procedures at MoF. Implement in full GFS (1997) TA mission recommendations.
Monetary accounts	Monthly reporting of balance sheets. Generally on time; 1.5-month lag	Acceptable but needs improvement: frequent reclassifications disrupt data consistency; misclassifications prevent meaningful analysis of the composition of NDA	Large and variable other items (net); frequent misclassification errors by commercial banks; numerous dormant items carried forward from the past; absence of adequate classification guidelines for Islamic modes of financing; after reclassifications in December 1999, quality of monetary data deteriorated significantly.	Provide TA on redesigning the balance sheets; train BOS statistical staff and banks' accountants; issue of new classification guidelines for banks in Arabic. Implement in full the 1999 TA mission on monetary statistics recommendations.

Type of data	Scope and timeliness of reporting	Adequacy for monitoring	Areas of concern	Steps to improve integrity
	Weekly flash reports of key monetary aggregates; 1-week lag	Good: new format introduced in 2000	Some divergence between reserve money in balance sheets and end-of month flash reports.	Include data on returns on investment deposits.
External sector Foreign exchange reserves	Monthly reporting of BOS active balances. Generally on time; 1.5-month lag	Good: data on BOS gross usable reserves seem complete and consistent with monetary accounts	Gross usable reserves are part of BOS active balances, which also include unusable reserves earmarked for particular purposes (such as oil, medicine and spare parts imports). The composition of the earmarked reserves and their potential usability in a case of a BOP need are not clear.	Clarify the items included in earmarked reserves.
Exchange rate	Upon request; minimal lag	Good: daily exchange rate available		
Balance of payments	Quarterly full BoP data provided on time and during missions; 3 month lag	Acceptable but needs improvement	Incompleteness of data on some services (oil transportation costs), investment income (oil related expenses and interest payments due on external public debt), transfers (workers' remittances), financial account (amortization due on external public debt) and FDI; large positive errors and omissions.	Introduce the revised reports form for commercial banks; improve data collection procedures; enforce the use of residency criterion; enhance institutional capacity of the BOS BoP compilation unit. Implement in full the recommendations of the 1999 TA in BoP statistics.
	Monthly trade data Upon request provided with a 2-3 month lag	Acceptable but needs improvement	Discrepancies between BOS data and customs data.	
External debt	Monthly payments to creditors. On time; 1.5-month lag	Good: BOS cash flow table is available.	BOS cash flow table does not reflect exactly actual payments made by the MOF.	Eliminate timing and recording discrepancies between the BOS and the MOF.
	Other debt data; 10-month lag	Good: coverage is comprehensive, although weaknesses in some areas persist.	BOS records are not reconciled with those of some creditors; data on ODA not available; interest on interest in arrears not calculated; for some creditors interest on arrears not separated from delayed interest.	Reconcile the data with creditors; further disaggregate the data according to standard definitions.

Sudan: Core Statistical Indicators as of April 30, 2000

	Exchange Rates	International Reserves	Central Bank Balance Sheet	Reserve/ Base Money	Broad Money	Interest Rates (Rates of Charge)	Consumer Price Index	Exports/ Imports	Current Account Balance	Overall Government Balance	GDP/ GNP	External Debt/ Debt Service
Date of Latest Observation	April 23, 2000	Feb 29, 2000	Feb 29, 2000	Feb 29, 2000	Feb 29, 2000	March 30, 2000	March 2000	Dec. 1999	Q4 1999	Jan. 2000	1997	1999
Date Received	April 24, 2000	Mission April, 2000	April 16, 2000	April 16, 2000	April 16, 2000	April 16, 2000	April 16, 2000	Mission April, 2000	Mission April, 2000	Feb.29, 2000	Mission April, 2000	Mission April, 2000
Frequency of Data	D	M	M	M/W	M	W	M/W	M	Q	M	A	A
Frequency of Reporting	W	M	M	M/W	M	M	M	M	Q	M	A	A
Source of Update	A (BOS)	A (BOS)	A (BOS)	A (BOS)	A (BOS)	A (BOS)	A (MOF)	A (BOS)	A (BOS)	A (MOF)	A (MOF)	A (BOS)
Mode of Reporting	C (Fax)	C (Fax)	C (Fax)	C (Fax)	C (Fax)	C (Fax)	C (Fax)	C (Fax)	C/V (Fax)	C (Fax)	C/V (Fax)	C/V (Fax)
Confidentiality	B	B	B	B	B	B	B	B	B	B	B	B
Frequency of Publication	M	M	M	M	M	M/W	M	M	Q	M	A	A

Abbreviations: Frequency: D-daily, W-weekly, M-monthly, Q-quarterly, A-annual. Mode of reporting: A-direct reporting by authorities; C-reporting by fax; V-staff visits. Confidentiality: B-for use by the staff and the Executive Board. BOS- Bank of Sudan, MOF-Ministry of Finance.

1/ (M) published monthly and (Q) quarterly in IFS, (W) weekly in BOS fact sheets. All data published annually in BOS Annual Report.

Sudan: Relations with the World Bank
(As of March 31, 2000)

1. The World Bank is currently engaged in non-lending services with Sudan; there is no active portfolio at present. Disbursements were suspended in April 1993, and Sudan's arrears were placed on non-accrual status in January 1994. Sudan's outstanding IBRD and IDA debt, including arrears, is some US\$1.2 billion; total accumulated IBRD and IDA arrears amounted to US\$140 million at the end of March 2000. Under current Bank policies, no lending is possible, pending full settlement of the arrears. Discussions on the normalization of relations were held during the Spring Meetings in 1999, and the Government agreed to start "good faith" payments of US\$1 million a month to the Bank, starting in July 1999. Payments for December 1999 were received on April 17, 2000. The rest of the monthly payments due since January 2000 are yet to be received.
2. The Government of Sudan (GOS) has expressed its eagerness for a resumption of Bank non-lending support, and the Bank has been responsive to the GOS on this request. The economic and sector work currently in progress is emphasizing areas relevant directly for poverty reduction, especially irrigation management, water resources and the social sectors. A joint team of Bank staff, GOS officials and local consultants have been working together to prepare a restructuring program for the Gezira Irrigation Scheme. Irrigation accounts for about 25 percent of total value added in the Sudanese economy; the Gezira is a major agricultural sector asset, representing about two-thirds of the total area of the large national irrigation schemes. The Gezira study is being coordinated with the activities of IFAD in Sudan. A draft report was discussed in a workshop attended by stakeholders in Khartoum in November 1999, and a final strategy and action plan is being finalized for dissemination and other follow-up actions. Bank staff has been working with the Sudanese authorities on the issue of water resource sharing and management involving countries along the Nile river. In the social area, the Bank has approved a grant from the Post-Conflict Fund to support a series of analysis of social sector issues, focusing on drinking water, education and health. A Bank mission has visited Khartoum to agree with the Government on the Terms of Reference for the social sector study, which is expected to cover both the North and the South. The first phase of the work would cover social expenditure patterns and policies, household coping strategies with economic distress and vulnerable groups. Other aspects of the study, including the status of displaced persons, would be initiated later.

Table 1. Sudan: Quantitative Quarterly Benchmarks, 1998-99

(In billions of Sudanese dinars, unless otherwise indicated)

	Dec 1998	Cumulative change in 1999 1/							
	Actual 2/	1st quarter		2nd quarter		3rd quarter		4th quarter	
		Program	Actual	Program	Actual	Program	Actual	Program	Actual
Benchmarks									
Banking system's NDC	119.8	6.8	2.9	11.0	8.2 10/	15.0	12.4 10/	18.0	15.0 10/
Domestic financing of the fiscal deficit 3/	...	3.5	2.4	6.0	5.2	8.0	10.9	10.0	13.2
New nonconcessional borrowing by government 4/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
BOS gross usable reserves (in millions of US dollars)	27.0	27.0	38.0	31.0	37.0	39.0	39.5	47.0	53.4
Payments to the Fund (in millions of US dollars)	0.0	13.0	13.2	22.0	22.2	31.0	31.3	40.0	40.3
Payments to non-Fund creditors (in millions of US dollars)	0.0	4.0	3.4	9.0	7.7	19.0	20.7	30.0	30.0
Social and development expenditure 5/		<u>Minimum floor on quarterly release</u>							
Federal budget transfers to the states on development account 6/	...	0.2	0.2	0.3	0.3	0.5	1.5	0.6	2.1
Federal development budget (local) 7/	...	3.5	3.5	7.5	9.5	12.2	16.0	16.6	22.3
Memorandum items									
Net domestic assets of the banking system	145.8	7.0	6.0	11.4	9.2	15.7	17.0	19.0	35.9
Reserve money 8/	111.8	6.0	15.7	11.5	18.9	17.7	21.5	22.2	38.5
Central government revenue	...	46.0	41.7	90.0	93.3	141.0	142.7	206.6	206.7
Disbursements of foreign assistance (in millions of US dollars) 9/	...	5.0	0.0	10.0	0.0	20.0	1.0	40.0	23.7

1/ Cumulative change since December 31, 1998.

2/ Outstanding stock at end-December 1998.

3/ Defined as net borrowing by the government from the Bank of Sudan (including changes in deposits of the central government with the BOS) and net sales of Government Musharaka Certificates.

4/ Loans will be deemed to be concessional when the currency-specific discount rate (determined by the market-related "commercial interest reference rates (CIRR)" as published by the OECD) applied to the contractual schedule of charges and principal payments, indicates a grant element of at least 35 percent.

5/ From Table 3 of EBS/99/64, 4/28/99.

6/ Total amount of transfers to the states on development account, including development expenditures on health, education, and safe drinking water, is budgeted at SD7.4 billion. Of this amount, nearly SD 6.28 billion is expected to be financed through external grants. The domestically financed component of transfers for development is budgeted at SD 1.12, of which 56 percent or SD 0.63 billion, is protected under the floor.

7/ Represents 75 percent of the total budgeted amount (SD 22.1 billion) in the Federal development budget, excluding capital transfers to public enterprises.

8/ Differs from monetary authorities' accounts because of reclassification of banks' holdings of CMCs to NDA.

9/ Disbursements from international and regional financial institutions to central government, over and above regular assistance from institutions, such as the UNDP, IDB, and IFAD.

10/ Differs from monetary survey because this figure excludes transitional deposits of public entities in commercial banks reclassified from other items (net) in April.

Table 2. Sudan: Status of Implementation of 1999 Structural Benchmarks

Policy Area		Status of Implementation
By End-March 1999		
I.	<i>External</i>	
	1. Begin calculating the official exchange rate on the basis of the five-day moving average exchange rate.	Done. Now being calculated as the median rate of the previous day.
II.	<i>Monetary</i>	
	1. Apply reserve requirements based on weekly average of reservable liabilities.	Done.
By April 1999		
I.	<i>Fiscal</i>	
	1. Implement first sales of the Government Musharaka Certificate (GMC).	Done.
By End-June 1999		
I.	<i>Fiscal</i>	
	1. Issue the government circular to implement the VAT by January 1, 2000, after the approval of the VAT law by Parliament.	Done.
	2. Begin the taxpayer registration program, after the approval of the VAT law.	Begun.
	3. Begin the implementation of action plan that would result in the adoption of a unified taxpayers identification program for large taxpayers in 1999.	Done.
	4. Line ministries will start preparing monthly accounts, which will be used to prepare the consolidated monthly government accounts.	Decree issued calling for line ministries to prepare monthly accounts and most do so.
	5. Establish a task force, consisting of members from the budget department, statistics department, the macro-fiscal unit, Chamber of Accounts, and some line ministries, to prepare an action plan for bringing the budget classification in line with the GFS standards.	Done.

Table 2. Sudan: Status of Implementation of 1999 Structural Benchmarks

Policy Area	Status of Implementation
II. <i>Monetary</i>	
1. Examine, with Fund technical assistance, the status of banks' compliance with key prudential regulations and develop an action plan for improving banking supervision.	Review conducted on May 17-30, 1999; plans to address bad loans being implemented as well as efforts to improve capital adequacy.
III. <i>External</i>	
1. Eliminate the remaining surrender requirements on cotton and gum arabic.	Done.
2. Eliminate Ministry of Commerce stamping of export and import contracts requirements.	Done.
3. Eliminate the export ban on raw skins and hides.	Done.
4. Eliminate the 2-day limit for the banks to sell foreign exchange.	Limit extended to one week on June 13, 1999, removed by end-February 2000.
By End-September	
I. <i>Fiscal</i>	
1. Complete the training of the operational staff in the VAT department.	Done. Basic training completed.
2. Submit VAT law to Parliament.	VAT Law approved by cabinet; Parliamentary action no longer required.
II. <i>Monetary</i>	
1. Begin using GMCs in open market operations.	Done.
By End-December	
I. <i>Fiscal</i>	
1. Provide preliminary data under GFS classification.	Done.
2. Adopt a unified taxpayer identification number for large taxpayers.	Done.
3. Introduce the VAT.	Postponed for June 1, 2000.

Table 2. Sudan: Status of Implementation of 1999 Structural Benchmarks

Policy Area		Status of Implementation
II.	<i>Monetary</i>	
	1. Enforce a unified methodology for calculating banks' incomes and profits.	Done.
	2. Agree with banks on measures to reduce the size of non-performing loans and ensure that provisioning is adequate.	Done.
	3. Agree with non-compliant banks of how to achieve appropriate capital adequacy ratio.	Discussions underway.
III.	<i>External</i>	
	1. Eliminate export taxes on cotton in the context of the 2000 budget.	Done.
	2. Adopt the first phase of the tariff reform, as described in the schedule attached to EBS/99/64, 4/28/99 in the context of the 2000 budget.	Done.
IV.	<i>Privatization</i>	
	1. Begin implementing the privatization plan described in the annex attached to EBS/99/64, 4/28/99.	Done.
V.	<i>Social sectors</i>	
	1. Prepare a timetable and action plan for making primary education compulsory.	Done.
VI.	<i>Other</i>	
	1. Adopt a revised Investment Encouragement Act, with a view to limiting exemptions and centralize the exemption granting authority.	Done. Implementing regulations which limit exemptions and centralize exemption granting authority have been passed.

Khartoum, May 7, 2000

Mr. Horst Köhler
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Mr. Köhler,

1. We are writing to inform you that we have completed our discussions with Fund staff on the fourth quarterly review of the first annual program under the medium-term staff-monitored program (MTSMP). The framework of the 1999–2001 MTSMP remains as described in our memorandum of economic policy (MEP) of April 26, 1999, and most recently updated in our MEP of February 12, 2000, which sets out an outline of the economic program for the year 2000. In the attached supplementary letter, we review performance under the program in October–December 1999 and the year 1999 as a whole, and update the economic and financial policy program for 2000.

I. IMPLEMENTATION OF THE 1999 PROGRAM

Macroeconomic developments

2. **The macroeconomic objectives** of the 1999 SMP have been broadly achieved. Based on the solid performance of the rainfed agriculture, livestock, and construction sectors, and the new oil investment and production, growth is estimated to have reached about 6 percent, continuing the trend performance of recent years. Tight demand management policies resulted in an average inflation rate for the year of 16 percent, somewhat exceeding the 14 percent program target. The external current account deficit contracted to about 3.5 percent of GDP (excluding interest due and public transfers) as higher than projected oil export prices helped to offset the weak performance of traditional non-oil exports. The Bank of Sudan (BOS) accumulated US\$53 million of usable reserves, US\$6 million more than programmed.

3. **Fiscal policy** in 1999 remained tight through the end of the year, with the overall deficit of 0.9 percent of GDP, less than targeted under the program. Throughout most of the year, constrained by uneven seasonal fiscal revenue patterns, expenditure was maintained below the program level. In addition, the surge in oil prices in late 1999 increased oil revenue above projected amounts. However, the expenditure restraint and higher oil revenue at end year were not sufficient to fully offset the shortfalls in customs revenue (due to lower than expected imports in the fourth quarter) and foreign financing, in addition to the unexpected relief expenditure following flooding. As a result, net domestic financing was slightly above target (by 0.1 percent of GDP).

4. Through end-December, **broad money growth** was roughly in line with the 1999 program. Reserve money, however, exceeded significantly the expected level for end-1999, possibly fueled by stronger than expected seasonal transaction demand for currency in December associated with Ramadan. While credit to government exceeded the benchmark level slightly, stagnation of credit to private sector (see paragraph 14 below) brought the overall domestic credit expansion in the banking system to below the benchmark level. However, net domestic assets (NDA) of the banking system exceeded the indicative benchmark substantially due to the higher than envisaged government borrowing and an increase in the accounting entries for the accrued interest on government debt done at end-December for the year as a whole. Inflation picked up to 17 percent on a twelve-month basis at end-year, due to stronger than expected spending pressures in Ramadan and ahead of the Eid-Al-Fitr holiday in early January. After some depreciation in the first half 1999, the exchange rate has remained broadly stable in nominal terms and the real exchange rate continued to appreciate through end-year.

5. The **external current account** outcome in 1999 was better than programmed. While high oil prices boosted export revenue, export prices for most traditional commodities declined further from the already low levels in 1998. The deficit on the overall balance was roughly as projected due to unexpectedly low private transfers and capital inflows.

Implementation of end-December 1999 structural measures

6. Final preparations are underway to enable the **introduction of the VAT** on June 1, 2000. Basic staff training is completed, an intensive public education program is ongoing, the majority of tax payers have registered, and a Ministry of Finance circular was issued in March announcing the June 1 start date to encourage the last nonregistered taxpayers to comply. The **pilot GFS reclassification** of data for 1998 has been completed. The **taxpayer identification number** was introduced for large taxpayers as scheduled in December 1999.

7. The BOS has agreed with banks on measures to **reduce the size of non-performing loans and to ensure adequate provisioning**. Technical assistance from the Fund, expected later this spring, will assist the BOS in monitoring agreements with non-compliant banks for achieving the **appropriate capital adequacy ratio**. In addition, banks are now applying a **unified methodology for calculating incomes and profits** based on a 1998 BOS circular requesting that all banks adopt the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) accounting principles.

8. We eliminated the **export tax on cotton and gum arabic**, the last remaining export taxes. In addition, **import tariff reform** was implemented as committed with the reduction of the maximum tariff to 60 percent, the reduction in the number of tariff bands to 4 and an average tariff of about 22 percent.

9. The 1999–2000 **privatization plan**, as agreed under the MTSMP (EBS/99/64, 4/28/99), is on track. Three enterprises are now at the point of sale, and the government share in the telecommunications company (Sudatel) has been decreased through the sale of shares

to the public to 58 percent from 68 percent with a further reduction through an additional tranche slated to be sold through the stock exchange in the next month. Implementing regulations for the **Investment Encouragement Act** have been approved which close loopholes by tightening the definition of goods to be exempted, providing the exemptions uniformly to all investors, and removing discretionary elements in application of the Act (see paragraph 20 below). Regarding social sector reform, a timetable for making **primary education** compulsory throughout Sudan is moving forward. Three states have now adopted compulsory primary education and the remainder has plans to introduce it by 2002, which will be difficult given the lack of resources.

II. MACROECONOMIC POLICIES FOR 2000

10. The economic objectives and policies of the government for the remainder of 2000 remain broadly as discussed in the February 2000 Memorandum of Economic Policies, including the objectives of real GDP growth of about 6.5 percent, a further decline in inflation, a narrowing of the external current account, and a buildup in official reserves. The macroeconomic policy mix to achieve these objectives centers on moderate fiscal adjustment, supported by a continuing cautious monetary policy stance. In light of the onset of oil production, we are now considering macroeconomic policy options in the context of a medium-term fiscal strategy that would allow our modest oil reserves to be best used in the public interest.

11. Fiscal policy remains central to our macroeconomic strategy. Our budget targets an overall deficit of 1 percent of GDP and limits central bank financing to 0.3 percent of GDP. However, in keeping with our commitments under the 2000 program, oil revenue above the budgeted projections will be only used to compensate for unexpected shortfalls in non-oil revenue and foreign financing, with the excess used to reduce net borrowing from the BOS. If current oil prices persist, we may be in the position to reduce the government net position with the BOS by a substantial amount. However, we remain concerned that **non-oil revenue** may fall short of projections due to possible undercollection during the initial stage of VAT implementation, the uncertain fiscal impact of trade reform, and the delays in reducing exemptions under the Investment Encouragement Act. Moreover, should it appear that the inflation target will be exceeded, the government stands ready to cut back expenditure as needed. Finally, we will carefully monitor implementation of the budget allocation for military expenditure, with a view to keeping it below budgeted levels if possible.

12. The rise in international oil prices through early 2000 has resulted in a continuing divergence between domestic and international prices for petroleum products, despite the increase in gas oil and gasoline prices in January. As a result, through end-March, the accumulated losses of the Sudan Petroleum Company (SPC) are estimated at about 17 billion dinars.¹ These costs have been largely covered through transfers from the budget in 1999, a

¹IMF staff estimates.

reduction in tax payments and profit transfers by the SPC, and access to SPC working capital. In April, due to the decline in world oil prices, we did not apply the agreed formula for pricing petroleum products (gasoline, gas oil, and LPG) for domestic use as we believe that domestic prices currently reflect the international oil price. It is expected the SPC's remaining accumulated losses would be recovered by end-June given the expected downward trend in world oil prices. For the future, domestic oil prices will be automatically adjusted in line with international prices on a quarterly basis. The new formula for sales by the government to the Khartoum refinery (which is expected to begin production in May) is based on the average world market price of the previous three months less pipeline costs plus the ten percent VAT. We will review the pricing mechanism over the next months, with the view to eventually liberalize domestic oil prices altogether.

13. Our **monetary policy** stance will remain broadly in line with that described in the February MEP, allowing for at least a doubling of official gross usable reserves to US\$98.4 million (still less than one month of imports) and an increase in real credit to the private sector by 27 percent. We will remain vigilant to the possible reemergence of inflationary pressures and will tighten demand accordingly. Should current expectations for world oil price trends prove correct, and barring unexpected exceptional circumstances, we should be able to increase reserves by a significant additional amount. While in the case of higher than projected oil revenue we will strive to fully match the increase in government deposits with an increase in BOS foreign currency reserves, we will also take into account exchange market conditions. We will review the adjuster mechanism with the staff at the time of the first review, taking into account the reduction in foreign currency reserves to the BOS following the start of operations at the Khartoum refinery.

14. At the same time, we are concerned with the protracted decline in recent years in **credit to the private sector**. Within the broader framework of improving soundness of the banking sector (discussed below), we will promote interbank competition and market information, further reduce reserve requirements, relax the remaining ceiling on credit for domestic trade, and cease to endorse the setting of minimum bank commissions and fees by commercial banks. In the next months, we are also planning amendments to laws, which have undermined banks' ability to collect overdue loans (paragraph 25). Finally, by end-2000 we will formulate a system of market-based incentives to strengthen the deposit base of banks. All of these steps should help reduce the cost and increase the availability of credit.

15. The BOS will continue its policies of maintaining a flexible **exchange rate** and deepening of the foreign exchange market. We believe that the current stability broadly reflects the emerging balance of supply and demand for foreign exchange due to the improvement of the economic environment and the return of business confidence. To promote interbank transactions, we removed the seven-day limit on commercial banks holding foreign exchange in February and increased the spread between buy and sell rates to 1 dinar. In addition, we will take steps to further develop the interbank foreign exchange market including through the removal of the limit on sales by exporters of foreign exchange earnings and improving the clearing system to ease banks' concerns that counterparties will not settle transactions on time. Against the background of moderately declining inflation and

nominal exchange rate stability, the real effective exchange rate appreciated moderately. Since the dinar has been undervalued in the past, we do not think that to date such an appreciation has had an adverse impact on the competitiveness of the traditional export sectors.

16. The government nonetheless keeps the **competitiveness** of the traditional traded sector under close review and thus far has not noted any negative impact from recent exchange rate stability on export competitiveness. We will complete a study on competitiveness of the traditional sectors by end-September 2000, with preliminary recommendations ready in May, and are considering steps for improving competitiveness through the reduction of costs, for example through increased government expenditure on roads. As part of our policy of removing structural rigidities in the agricultural sector that impede productivity, we will consistently enforce the ban on ad-hoc interstate trade taxes on agricultural products.

III. STRUCTURAL REFORM MEASURES

17. We are committed to implementing the structural measures envisaged under the MEP for 2000. Regarding fiscal sector reforms, on **tax administration reform** we anticipate some transitional difficulties in the early stages of implementing the VAT, for which we would welcome continued technical assistance from the Fund. We are taking additional steps in improving **public expenditure management** through the full GFS classification of revenue, expenditure and financing with technical assistance from the Fund in spring 2000 and a proposal for bringing forward the timing for GFS reclassification of the government accounts to end-2000 will be submitted to the Council of Ministers shortly.

18. In the field of the **financial reforms**, with the successful redemption of the first GMC tranche, public confidence in this new instrument is gradually improving. To further deepen the interbank market, the government will elaborate a new strategy, including the promoting of a net of market makers in GMCs and CMCs, and developing a new Ijara-based Islamic security tradable in the market. The government will also consider additional transfers of GMCs to the BOS within the program ceiling on government borrowing to enhance its ability for indirect monetary management. The BOS has already reduced the number of credit windows from 3 to 2 (an end-March benchmark) and has started auctioning credit to banks on a competitive basis. The BOS is considering introduction of a new Muzara'a-based mode of Islamic to supplement Salam financing as the principle credit instrument for agricultural financing. The BOS will also narrow the gap between reserve requirements on domestic and foreign currency deposits to eliminate the distortionary bias and to augment the liquidity of the banking system by September 2000. To further financial liberalization, by the same date, the BOS will relax the credit ceiling on domestic trade, the last remaining binding ceiling.

19. We consider enhancing **bank soundness** key to achieving our macroeconomic objectives. The BOS is working with banks on measures to reduce the size of non-performing loans and is considering raising provisioning requirements to ensure sufficient coverage of doubtful loans. We have established the minimum level paid-in capital at

SD 3 billion and announced plans to assure banks' compliance with an appropriate capital adequacy ratio, including the introduction of incentives and penalties for non-compliant banks. Given the complexity of the tasks ahead, which we expect will also include some consolidation of banks, we have requested further long-term technical assistance from the Fund in the area of bank restructuring.

20. Regarding **trade reforms**, under the revised Investment Encouragement Act which became effective in April, all inputs are exempted from customs tariffs. In addition, capital input goods are exempt from the VAT, although the VAT continues to be applied to all other inputs at the uniform rate of 10 percent. Input goods have been narrowly redefined to exclude any goods with alternative uses in the retail market. In addition, previous exemptions given to investors for textiles, tires and saloon cars are abolished, and the customs tariffs on textiles and industrial-use tires reduced to provide an even playing field. All the new exemptions and customs tariff rates now apply uniformly to all investors of these products. We also intend to reconsider the role of export councils and of the list of essential goods, which can be imported using bank credit facilities.

21. As to reform of the **foreign exchange regime**, based on a review of the interbank foreign exchange market, the BOS will take further steps to deepen the foreign exchange market, including by widening the spread between its buy and sell rates to 0.5 percent by June 2000, and removing the limits on exporters' holdings of foreign exchange by December 2000.

22. In the **social sector**, the government will further pursue its plan for introducing countrywide compulsory primary education. The government is also beginning to formulate a poverty reduction strategy paper. At the same time, we will continue to work closely with the World Bank on studies on poverty, social services (water, education and health), displaced people, and vulnerable groups. Once completed, these studies will be the basis for action programs for more effective reduction of poverty and delivery of social services.

23. Given the importance of **agriculture** for the Sudanese economy (about 40 percent of GDP), we will continue working with the World Bank on preparing a reform program for the Gezira irrigated scheme. Indeed, we have already agreed for one part of the Gezira scheme to participate in a pilot project that would allow farmers greater choice regarding crop patterns and water use. Moreover, the Ministry of Agriculture has recently announced a policy under which farmers will no longer be required to produce cotton (the last compulsory crop). A committee chaired by the Minister of Justice has been established with the mandate of ensuring compliance of all state governments with the earlier decision to limit taxes on agricultural products and to enforce the removal of taxes on interstate agricultural trade.

24. We will continue structural reforms in the **electricity sector** aimed at improving efficiency, stability of power supply, and meeting the growing demand of the economy for electricity. In 2001, we will remove the remaining consumer subsidies and will revise the tariffs accordingly. To cut the cost of power supply, we intend to reduce technical and nontechnical losses, continue our policy of retrenchment (we have already reduced personnel

from 17,500 to 10,500) and upgrade training, take steps to attract private—local and foreign—investors, and encourage independent power producers. In addition to continuing implementation of the 1999–2000 **privatization** program, we will explore the proposed restructuring of the electricity sector, such as divestiture of non-core functions in addition to opening the electricity sector to private investors.

25. Overall, we believe the **regulatory framework** in Sudan to be broadly satisfactory. In the context of a **judiciary reform**, the government plans to revise the Bankruptcy Law and the Law on Auctioning Mortgaged Assets to allow banks to own assets of defunct debtors. By June 2000, the government will approve the revised Statistical Act to include provisions enforcing timely and comprehensive data submission by economic agents to the Central Bureau of Statistics. To ease legal impediments to financial intermediation, we intend to revise other legal provisions which may undermine banks' ability to collect overdue loans and discourage extension of new credit to the private sector.

26. We remain committed to data openness and statistical transparency and reaffirm our determination to solve the persistent **statistical problems**, which hamper economic policy decision-making. The institutional capacity of the Central Bureau of Statistics (CBS) will be strengthened to allow it to begin introduction of the 1993 System of National Accounts (SNA). The CBS will also finalize a number of surveys underway (on industry, energy consumption, and social sector issues), and start preparations for conducting a census of agricultural production and a household income and expenditure survey. With IMF technical assistance and in cooperation with commercial banks and certified accountants, the BOS will vigorously address the classification problems in its balance sheet and in the consolidated balance sheets of commercial banks, as outlined in the February MEP. As to balance of payments statistics, the BOS will revise reporting forms for commercial banks, enforce use of the residency criterion, and enhance institutional capacity of the BOP compilation unit. Responding to the growing demand for information from the private sector, the BOS will establish a web site on the Internet.

IV. RELATIONS WITH CREDITORS

27. The government reaffirms its commitment to a repayments schedule to the **Fund** of US\$60 million in 2000; this is a very heavy burden for the country, especially when other creditors are willing to provide new funds on the basis of limited payments. Nevertheless, if warranted by balance of payments developments, we will consider increasing payments to the Fund above the specified level later in 2000. Despite the increase in payments to the Fund, we will attempt to increase payments to other creditors to US\$60 million but will need to review this decision again based on the updated oil revenue projections and the outcome of negotiations with other creditors. We have committed to resume payments to the World Bank at the previously agreed levels which had been temporarily suspended earlier this year until our overall payments obligations were clarified.

28. We welcome the recent Executive Board decision and the efforts undertaken by the Fund staff in developing an external debt workout scenario which could lead to a

comprehensive resolution of Sudan's arrears to the Fund in the context of a Rights Accumulation Program, once financing assurances become available. Finally, we would again like to extend our appreciation for the continuous efforts made toward helping Sudan implement its economic reform program, improve cooperation with the Fund, and begin to normalize relations with external creditors.

Sincerely yours,

/ s /
Saber Mohammed Hassan
Governor, Bank of Sudan

/ s /
Mohamed Kheir Al-Zubeir
Minister of Finance and
National Economy

Table 1. Sudan: Quantitative Quarterly Benchmarks, 1999–2000

(In billions of Sudanese dinars, unless otherwise indicated)

	Dec. 1999	Cumulative change in 2000 1/			
	Actual 2/	1st quarter	2nd quarter	3rd quarter	4th quarter
Benchmarks					
BOS net domestic assets	142.3	6.3	5.4	7.4	7.1
Government budget: current expenditure	...	62.3	124.6	191.6	268.0
capital expenditure	...	12.6	29.0	46.0	65.9
Domestic financing of the fiscal deficit 3/ 4/	...	3.5	5.6	7.9	9.1
BOS financing	...	3.0	5.0	7.0	8.0
Net sales of GMCs	...	0.5	0.6	0.9	1.1
New nonconcessional borrowing by government 5/	0.0	0.0	0.0	0.0	0.0
BOS gross usable reserves (in millions of US dollars) 4/	53.4	53.4	63.4	78.4	98.4
Payments to the Fund (in millions of US dollars)	...	15.0	30.0	45.0	60.0
Minimum floor on quarterly release					
Central government social and development expenditure					
Social expenditures 6/	...	12.1	25.9	41.3	59.2
Local development expenditures 7/	...	5.4	13.4	24.1	39.0
Memorandum items					
Net domestic assets of the banking system	183.1	9.5	16.8	23.6	28.0
Reserve money	152.4	8.1	11.6	19.3	26.1
Central government non-oil revenue	...	48.6	104.4	166.9	240.6
Central government oil revenue	...	15.9	31.8	47.7	63.6
Payments to non-Fund creditors (in millions of US dollars)	...	15.0	30.0	45.0	60.0

1/ Cumulative change from December 31, 1999.

2/ Outstanding stock at end-December 1999.

3/ Defined as net borrowings by the government from the Bank of Sudan (including changes in deposits of the central government with the BOS) and net sales of Government Musharaka Certificates (GMCs).

4/ To the extent that any oil revenue above the projected level in the budget are not needed to compensate for the projected amounts of non-oil revenue and foreign financing in the budget, it is expected that it would be used to reduce net borrowing from the BOS with a counterpart increase in official reserve accumulation.

5/ Loans will be deemed to be concessional when the currency-specific discount rate (determined by the market-related "commercial interest reference rates (CIRR)" as published by the OECD) applied to the contractual schedule of charges and principal payments, indicates a grant element of at least 35 percent.

6/ Central government expenditure on research, enhancing institutional capacity, and social support.

7/ Central government expenditure on removing agricultural bottlenecks, roads, transportation, and electricity.

Table 2. Sudan: 2000 Structural Benchmarks

Policy Area
End-March 2000 <i>Fiscal</i> 1. Agree on a formula for automatic quarterly adjustment of domestic petroleum prices in line with international prices.
<i>Monetary</i> 1. Reduce number of credit windows from 3 to 2 (one week liquidity window and "general" window). 2. Establish the size of the minimum paid-in capital of banks.
End-June 2000 <i>Fiscal</i> 1. Implement the VAT (June 1).
<i>External</i> 1. Widen the spread between buying and selling rates to 0.5 percent. 2. Review adequacy of mechanisms set up by commercial banks to monitor exports and impact of these mechanisms on exporters.
<i>Monetary</i> 1. Develop an incentive scheme and agree with noncompliant banks on plans to achieve the appropriate capital adequacy ratio.
<i>Statistics</i> 1. Revise the Statistical Act enforcing data submission by economic agents to the Central Bureau of Statistics. 2. Revise the balance sheet of the BOS and the consolidated balance sheet of commercial banks with the view to improve classification and reduce other items (net).
<i>Other</i> 1. Approve executive regulations limiting customs exemptions under the Investment Encouragement Act to one year.

Table 2. Sudan: 2000 Structural Benchmarks

<p>End-September 2000</p> <p><i>External</i></p> <ol style="list-style-type: none"> 1. Complete a study of competitiveness and ways for improving productivity of the traditional export sectors.
<p><i>Agriculture</i></p> <ol style="list-style-type: none"> 1. Prepare plan and agree on timing for the reform of the Gezira scheme.
<p><i>Other</i></p> <ol style="list-style-type: none"> 1. Submit revised law on auctioning mortgaged assets to allow banks to own assets of defunct debtors.
<p>End-December 2000</p> <p><i>Fiscal</i></p> <ol style="list-style-type: none"> 1. Reconcile monthly accounts prepared by the Chamber of Accounts with the accounts of ministries with the BOS and start using them for fiscal reports to the Fund.
<p><i>External</i></p> <ol style="list-style-type: none"> 1. Reduce the maximum import tariff from 60 percent to 40 percent. 2. Reduce the average tariff to below 20 percent. 3. Reduce the number of tariff bands from 4 to 3. 4. Eliminate the 20-day limit on exporters' holding foreign exchange.
<p><i>Regulatory</i></p> <ol style="list-style-type: none"> 1. Submit revised bankruptcy law to Parliament.
<p><i>Other</i></p> <ol style="list-style-type: none"> 1. Agree with World Bank on action plans for alleviating poverty and social service, delivery as well as improving the situation of most vulnerable groups of society, including displaced persons. 2. Complete implementing the privatization plan described in the annex attached to EBS/99/64, 4/28/99.

**Statement by the IMF Staff Representative
May 22, 2000**

This statement provides information on recent economic developments in Sudan that has become available since the circulation of the staff report on the Article IV consultation and the fourth review of the first annual program under the medium-term staff-monitored program (EBS/00/83, 05/08/2000). This information is preliminary and will be discussed by the mission scheduled to visit Khartoum in early June to conduct the first review of the second annual program under the medium-term staff-monitored program. The updated information does not change the thrust of the staff appraisal.

I. MACROECONOMIC DEVELOPMENTS

- The inflation rate eased to 11.9 percent in April on a twelve-month basis, continuing the trend decline from the end-December 1999 peak of 17 percent.
- Early budget data indicate that the quarterly fiscal benchmarks for end-March were met. Current and capital expenditures were within the agreed cap. Stronger than programmed oil revenue more than offset shortfalls in revenue from fees and charges. Tax revenue was broadly on target as the existing excise and trade tax structure has been kept in place pending the delayed introduction of the VAT on June 1. Preliminary calculations for the adjuster indicate that the ceiling on domestic financing of the fiscal deficit was also met.
- In January, Bank of Sudan (BOS) gross usable reserves increased by US\$7 million to US\$60.5 million as of end-January 2000.
- Net domestic assets of the BOS through end-February were considerably below end-March program levels as the net claims on the government were roughly unchanged from end-1999 and the net position with commercial banks declined.
- The exchange rate of the Sudanese dinar against the U.S. dollar remained stable through end-April.

II. STRUCTURAL MEASURES

- On May 9, 2000, the BOS announced the unification of reserve requirements. The reserve requirement on deposits in domestic currency was decreased from 20 to 15 percent, while the reserve requirement on deposits in foreign currency was raised from 10 to 15 percent. Commercial banks will have until July 1 to comply.

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Additionally, the unified minimum rates on commercial banks' services were abolished and, to encourage competition, the BOS will begin to publish the rates charged by each bank. Finally, the minimum profit margin under Murabaha contracts was decreased from 18 to 15 percent.

III. RELATIONS WITH CREDITORS

- In January–April, 2000, the authorities adhered fully to the schedule of monthly payments to the Fund.



INTERNATIONAL MONETARY FUND

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June 9, 2000

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Sudan

On May 22, 2000, the Executive Board concluded the Article IV consultation with Sudan.¹

Background

Cooperation between Sudan and the IMF continues within the framework of a medium-term staff-monitored program (MTSMP) for the period of 1999–2001. The MTSMP is based on the government's economic recovery strategy and builds on the progress achieved in the implementation of the 1997–98 annual staff-monitored programs (SMP), including in reducing financial imbalances, strengthening taxation, improving public expenditure management, financial deepening, exchange rate unification, foreign trade liberalization, and privatization. The objective of the MTSMP is to lay a solid foundation for sustained economic growth through a further improvement in the macroeconomic situation supported by implementation of structural reforms to enhance resource allocation and encourage private sector activity. The program establishes medium-term targets of annual real growth of 5–6 percent, a reduction in average inflation to 5 percent, a further narrowing of the current account deficit, and a substantial buildup of gross usable reserves.

In 1999, the Sudanese authorities broadly achieved the macroeconomic objectives of the first annual program under the MTSMP. Based on solid performance of rainfed and non-traditional crops, livestock, and the new oil sector, growth is estimated to have reached about 6 percent. Tight fiscal and monetary policies allowed the government to successfully reduce inflationary pressures and to bring the average inflation rate down, for the third consecutive year, to 16 percent. After averaging about 8 percent of GDP in recent years, the external current account deficit contracted to 3.5 percent of GDP (excluding interest due and public transfers) as

¹ Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

higher than projected oil prices helped to offset the weaker performance of traditional exports. By end-1999 the Bank of Sudan (BOS) doubled its usable foreign exchange reserves, to US\$53 million, exceeding the target by US\$6 million.

Structural reforms moved forward in 1999 and early 2000. The tax authority has finalized preparations for the June 1, 2000 start date for the Value Added Tax (VAT). Implementing regulations for the revised Investment Encouragement Act have been passed. Exchange market reforms continue. The BOS has introduced instruments for indirect monetary management, although their monetary impact remains limited. The BOS has announced a new bank restructuring strategy and is addressing the issue of nonperforming loans.

Despite the progress achieved, the overall economic situation remains fragile and susceptible to exogenous shocks. Determined policy implementation by the government is needed if the objectives of the MTSMP are to be met. Public expectations and political pressures for immediate use of oil revenues are high. However, the oil revenue windfall by itself will not be enough to sustain even required increases in spending, such as in the social and development sectors. For the near future, Sudan will remain a predominantly agricultural economy, facing financing shortages, a deteriorated infrastructure, recurrent problems with flooding, an inappropriate institutional framework in the irrigated sector, and a secular decline in world commodity prices. The banking system is weak, with many banks undercapitalized, and is not capable of supporting private sector growth. Poverty, especially in the South, is extremely high. Finally, Sudan's external debt, estimated at US\$24 billion at end-1999 and most of it in arrears, is unsustainable.

Against this background, the program for 2000 aims at cementing the macroeconomic gains of the previous years, while expanding the breadth and depth of the structural reforms. Real GDP growth is targeted to reach 6.5 percent. New oil revenue will allow the government to reduce its borrowing from the BOS and leave more room for credit to the private sector. The resulting lower monetary expansion will help to relieve inflationary pressures and to achieve the 9 percent end-of-year inflation target. In line with expected improvements in the balance of payments, Sudan's gross usable reserves will increase by US\$45, doubling the level at end-1999. On the structural side, the program pursues the goal of strengthening the budget by introducing a VAT and improving expenditure management through establishing accounts classification compatible with international standards. The government intends to start automatic adjustments of domestic oil prices in line with international prices. Financial sector reforms include bank consolidation and restructuring, enforcing capital adequacy requirements, reduction of nonperforming loans, and further development of indirect monetary management instruments. The program also envisages a wide range of other structural reforms, such as further trade and exchange market liberalization and privatization. The government has committed to US\$60 million in payments to the IMF in 2000. The authorities are also working with the World Bank to develop policies that would eventually enhance the social safety net, strengthening health and education systems and reducing poverty.

Executive Board Assessment

Executive Directors noted the progress achieved by Sudan over the past three years in stabilizing the macroeconomic situation, moving forward the structural reform agenda, and improving relations with creditors against a background of a difficult domestic and international environment. Directors generally considered that Sudan's performance under the staff-monitored program (SMP) in 1999 had been satisfactory both in terms of policy implementation and payments to the Fund. Nevertheless, they noted that the overall macroeconomic policy stance had not yet succeeded in reducing inflation adequately, and there had been delays in implementing some of the key reforms. Looking ahead, Directors urged the authorities to consolidate and sustain the improvement in the macroeconomic situation, to push forward their agenda of structural reforms in order to enhance confidence and the expansion of the private sector, and to ensure careful management of Sudan's new oil resources. Directors also emphasized the contribution that a peaceful resolution of the armed conflict would make to poverty alleviation and improvements in social indicators.

In considering the outlook for 2000, Directors urged the authorities to be vigilant against the possible reversal of the recent improvements in the inflation rate and to proceed with caution in implementing the program by minimizing central bank financing of the budget and restraining expenditure as needed to keep inflation on track. Directors strongly emphasized the importance of ensuring that higher oil revenues not undermine budgetary discipline, and, in this regard, they welcomed the commitment to use excess oil revenues to reduce net borrowing from the Bank of Sudan. Moreover, they cautioned against increasing entitlement programs, which would be difficult to unwind should oil prices weaken. Directors also noted the need to continue to broaden the tax base and improve collection of non-oil revenue. In this connection, they welcomed the indication that the VAT will be put in place as planned on June 1. Directors underscored that cuts in nonproductive, and especially military expenditures would greatly facilitate the achievement of social objectives consistent with overall strength in the fiscal position.

Directors observed that no major pressure on the exchange rate was evident, despite the virtual stability in the rate in recent months. However, in view of the many challenges and risks facing Sudan's economy and the still low level of international reserves, Directors encouraged the authorities to allow the exchange rate to move flexibly in response to market forces and not to allow any perception to develop in the market that the rate was effectively fixed. In this regard, Directors considered that efforts should be stepped up to further develop the interbank foreign exchange market. Directors encouraged the authorities to closely monitor developments in external competitiveness, and, in particular, to avert any threat of oil-induced strength in the exchange rate undermining the competitiveness of the non-oil sector.

Directors welcomed the recent measures taken by the Bank of Sudan to strengthen the financial and banking sector, including the recent unification of the reserve requirements on domestic and foreign currency deposits, and urged the authorities to continue their program on an accelerated basis. They drew attention to the recent decline in credit to the private sector, observing that its reversal—in line with the program—would be an essential prerequisite for

future economic growth. To that end, Directors agreed with the package of measures prepared by the authorities to address this problem, including the updating of laws to remove impediments to the extension of credit, strengthening provisioning and compliance with prudential regulations, and improving performance with respect to loan recovery. Directors encouraged the provision of Fund technical assistance to assist the authorities in these areas.

In other structural reform areas, Directors were encouraged by the measures taken recently—in particular, the approval of the implementing regulations for the Investment Encouragement Act—but urged the authorities to avoid any further delays in implementation. Directors were concerned with the continuing delays in adjusting petroleum product prices and recouping the remaining losses of the Sudan Petroleum Company. They stressed that it would be important for the authorities to utilize the agreed automatic petroleum price mechanism. Directors advised the authorities to move to full market liberalization in the petroleum product sector as quickly as possible.

The commitment to transparency in the oil sector to date was welcomed, and Directors strongly urged the authorities to build on this by full public disclosure of oil revenue data and periodic internal audits.

Taking a longer-term perspective, Directors were in general agreement with the medium-term macroeconomic targets for the SMP, noting that these were based on continued structural reforms across many sectors, and in particular the financial and agricultural sectors. At the same time, they recognized the risks to the program from structural weaknesses in the economy, such as low investment in physical and human capital, deteriorating infrastructure in the agricultural sector, and an unsustainable debt burden.

Directors noted Sudan's adherence to the schedule of payments to the Fund through April 2000, and urged the authorities to continue this performance. Welcoming the continued improvement in relations with external creditors, they also urged that further progress be made toward an eventual resolution of Sudan's external debt problem.

Directors welcomed the authorities' intention to strengthen the statistical database, especially regarding monetary statistics where some problems had emerged.

Public Information Notices (PINs) are issued, (i) at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies; and (ii) following policy discussions in the Executive Board at the decision of the Board. As part of a pilot project, the staff report for the 2000 Article IV consultation with Sudan is also available.

Sudan: Selected Economic and Financial Indicators, 1996–1999

	1996	1997	1998	1999
(Annual changes in percent)				
Domestic economy				
Real GDP growth	4.0	6.7	5.0	6.0 ^{1/}
End-of-period CPI inflation	114.2	32.0	7.9	17.0
Average CPI inflation	132.8	46.7	17.1	16.0
(In percent of GDP)				
Financial variables				
Total revenue	6.3	6.6	7.9	8.5
Total expenditure	9.8	7.4	8.6	9.3
Current expenditure	9.2	6.8	7.8	8.0
Capital expenditure	0.6	0.6	0.8	1.3
Overall balance (cash)	-3.5	-0.7	-0.7	-0.9
Broad money (change in percent)	6.5	37.0	29.6	24.6
Reserve money (change in percent)	81.8	34.3	29.4	35.1
(In millions of U.S. dollars)				
External sector				
Exports, f.o.b.	620	594	596	780
Imports, c.i.f.	-1,547	-1,580	-1,925	-1,412
External current account balance ^{2/}	-579.6	-330	-338	-236
In percent of GDP	-7.6	-4.0	-3.9	-2.4
Real effective exchange rate (change in percent)	6.7	22.0	-25.8	18.8

Sources: Data provided by the Sudanese authorities, IMF staff estimates.

1/ Preliminary

2/ Excluding interest due, public transfers, and oil pipeline imports.

**Statement by J.P. de Morais, Executive Director
for Sudan
May 22, 2000**

1. The 2000 Article IV discussions centered on the progress Sudan was making in the implementation of its medium-term staff monitored program (MTSMP). It was also the occasion to consider the adequacy of policies for remainder of the year. On either count, it is heartening to note that, despite the continuing difficult external environment, the recent severe natural disasters, the lack of meaningful financial support, and the still unresolved civil conflict, Sudan has made notable progress towards macroeconomic stability and introduced important reforms that underpin strong economic growth in recent years.

2. It is encouraging to note therefore that the macroeconomic objectives for 1999 have been broadly achieved with the rate of growth, at about 6.0 percent, remaining significantly strong for the third consecutive year. This rapid pace of growth, even by international standards, was led by the solid performance in agriculture, livestock and construction sectors. The coming on stream of oil production also helped to boost growth in 1999. Meanwhile, the pursuit of prudent financial and economic policies have resulted in a significant slowdown in the rate of inflation in recent years although pressures re-emerged at the end of the year due to seasonal factors, including in particular the higher-than-expected demand for currency associated with Ramadan. The external current account narrowed reflecting in part the higher oil export prices. In the event, Sudan accumulated reserves beyond program projections by US \$ 6 million. However, it is apt to point out that, at only 0.5 months of import cover, the external payments situation remains very precarious.

3. The overall fiscal deficit, at 0.9 percent of GDP in 1999, was lower than programmed and serves to further demonstrate the government's commitment to its fiscal consolidation program. It is important to bear in mind that this was achieved by containing expenditure below the program level in the face of uncertain revenue outcome. In this connection, it should also be noted that thus far there are no indications that the increase in oil revenues have resulted in higher expenditure even though the need for reconstruction and the provision of essential social services remain large and urgent. Meanwhile, the authorities recognize the need to strengthen non-oil revenues through among others , implementing necessary reforms, including in particular the prospective introduction of VAT in June 2000.

4. The conduct of monetary policy was complicated by the stronger-than-expected seasonal factors already mentioned, the transaction demand for currency associated with Ramadan in December 1999 which led to the pick up in inflation at the end of the year. In the meantime, financial sector reforms are continuing. The Government Musharaka Certificate (GMC) tranche was successfully redeemed and there are encouraging signs that confidence

in this new instrument is improving. Also, steps have been taken to strengthen the banking sector, including in particular efforts to reduce non-performing loans and ensure adequate provisioning. At the same time, all banks have been requested to adopt the accounting principles of the Accounting and Auditing Organization for Islamic Financial Institutions.

5. As regards structural reforms, it should be noted that the export tax on cotton and gum Arabic has been eliminated, actions which should help to reinforce external competitiveness. The import tariff reform has been implemented according to schedule with the reduction of the maximum tariff to 60 percent and the number of tariff bands to four. The privatization of state owned enterprises is broadly on track with three companies now on point of sale. In addition, the sale of shares in the telecommunications company (Sudatel) has reduced the level of Government interest and further sales will be made through offers on the stock exchange in June. The Investment Encouragement Act has been approved and should help to streamline customs exemptions to ensure uniform treatment to all investors and remove elements of discretion. In the area of social services, plans are already underway to make primary education compulsory in the country. Thus far, three states have already adopted this plan and the remainder will introduce it by 2002.

6. The program for 2000 was considered extensively by the Board during the discussion in February. The main objectives and economic policies have not changed: real GDP is expected to strengthen further to about 6.5 percent and inflation will be reduced to the single digit level. The external current account will continue to decline, allowing a further build up of reserves.

7. As discussed in the Memorandum of Economic Policies, the budget will remain the focus of macroeconomic strategy with the overall deficit programmed at 1.00 percent of GDP and central bank financing will be limited to only 0.3 percent of GDP. The Government, which has taken efforts to ensure transparency, has reaffirmed that oil revenues above budgeted projections will be used to offset shortfalls in non-oil revenues whose performance remains uncertain, especially with the introduction of VAT, the impact of trade reforms and the delays in reducing exemptions already mentioned. In any event, if current prices persist, government indebtedness to the Bank of Sudan will be reduced.

8. As already stated, monetary policy will focus on bringing inflation further down, consistent with the objective of gradually strengthening the external sector through further build up of reserves to at least one month of imports. Following its decrease in 1999, it is expected that private sector credit will increase in the period ahead. In part, this is being promoted by steps to improve the soundness of the banking sector, the promotion of interbank competition and market information, the reduction of the reserve requirements, the and the relaxation of the remaining ceiling on domestic credit. The Bank of Sudan has reiterated its intention to maintain a flexible exchange rate and to deepen the foreign exchange market. While the improved economic environment and the emerging business confidence underlies the stability now prevailing in the foreign market, the authorities are monitoring developments closely. The authorities hold the view that recent moderate appreciation of the real effective exchange rate has not affected the country's external competitiveness. Meanwhile, action is being taken to promote interbank transactions with the

removal of the seven-day limit on commercial holding of foreign exchange in February and the increase in the spread between the selling and buying rates.

9. As already indicated, the reform agenda is being implemented as planned in key sectors, including agriculture, fiscal and financial sectors as well as the privatization of state enterprises. These reforms are aimed at promoting economic efficiency by increasing the role of private sector investment. These efforts are being reinforced by regulatory framework which remains broadly appropriate. Nevertheless, plans are underway to revise the Bankruptcy Law and the Law on Auctioning and Mortgage Assets with a view to allowing banks to assume the ownership of assets of defunct debtors. To improve the collection of statistical data, the revised Statistical Act will provide for enforcing the timely and comprehensive submission of data by economic agents to the Central Bureau of Statistics. In this connection, the authorities have reaffirmed their commitment to address the statistical problems with technical assistance from the Fund and other competent international organizations, especially for the System of National Accounts.

10. Finally, the Government has reiterated its commitment to the payments schedule to the Fund as had been agreed in February. The authorities have emphasized that this remains a major burden to the country, especially when considering that other creditors would resume lending if Sudan were to make only modest payments. This reaffirmation once again demonstrates their desire to restore their voting and related rights in the Fund as further important step towards the full normalization of relations. They strongly believe that this will eventually unlock the much needed assistance for a comprehensive resolution of their external indebtedness.

11. To conclude, I believe that the first annual program under the MTSMP has been successfully implemented and the authorities are proceeding to consolidate the gains made so far. They recognize that this provides the path for reinvigorating growth as has been witnessed in the last few years under successive economic adjustment programs.