

INTERNATIONAL MONETARY FUND



Staff Country Reports

Sudan: 2006 Article IV Consultation and Staff-Monitored Program—Staff Report; Staff Statement; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for Sudan

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2006 Article IV consultation with Sudan and the staff-monitored program, the following documents have been released and are included in this package:

- the staff report for the 2006 Article IV Consultation and Staff-Monitored Program, prepared by a staff team of the IMF, following discussions that ended on February 9, 2006, with the officials of Sudan on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on April 19, 2006. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- a staff statement of May 3, 2006 updating information on recent developments.
- a Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its May 3, 2006 discussion of the staff report and the staff-monitored program.
- a statement by the Executive Director for Sudan.

The documents listed below have been or will be separately released.

Letter of Intent sent to the IMF by the authorities of Sudan*

Memorandum of Economic and Financial Policies by the authorities of Sudan*

Technical Memorandum of Understanding*

*Also included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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SUDAN

Staff Report for the 2006 Article IV Consultation and Staff-Monitored Program

Prepared by the Middle East and Central Asia and
Policy Development and Review Departments

Approved by Lorenzo L. Pérez and Carlo Cottarelli

April 19, 2006

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EXECUTIVE SUMMARY

Sudan's economic performance in recent years has been good despite internal conflicts and the difficulties of concluding and implementing the peace agreement with the South. Growth has been robust, inflation has been kept at a single-digit level, and important reforms have been undertaken. There has been progress with financial sector reforms and trade liberalization, and the managed floating exchange rate regime has been working well. Notwithstanding these achievements, several challenges remain to make the Government of National Unity fully operational, achieve peace throughout the country, and implement additional reforms to sustain growth and stability and deal with widespread poverty.

The economic program for 2006 addresses some of those challenges. Despite an increase in oil revenues, the fiscal space of the central government will be constrained because of the transfers required by the peace agreement and decentralization. These transfers, coupled with higher capital expenditures, will contribute to a substantial increase in pro-poor development spending. In this context, and to safeguard macroeconomic stability, an additional reorientation of expenditures is required, including through a reduction in fuel subsidies.

Sudan's economic prospects are favorable, assuming a continuation of the reform effort. Critical actions going forward are as follows:

- Adhere to fiscal spending and reserve money targets in an environment of exchange rate flexibility to keep inflation in check.
- Introduce a new national currency to foster financial development in the South and economic integration.
- Ensure close coordination between the government of Southern Sudan, the other states, and the central government to harmonize spending and preserve macroeconomic stability.
- Initiate fiscal reporting according to Government Finance Statistics Methodology and publish detailed oil-sector data to improve expenditure management and transparency.
- Build capacity, transparency, and accountability at all levels of government and make the Fiscal and Financial Allocation and Monitoring Commission operational to support fiscal decentralization.
- Proceed with reforms to remove structural rigidities and lower transactions costs in order to improve competitiveness.

Sudan's external debt problems continue to limit the country's access to external development financing. Despite these and other emerging constraints, the staff has urged the authorities to maintain their record of cooperation on economic policies and payments to the Fund including minimizing nonconcessional borrowing in order to facilitate the prompt resolution of Sudan's debt and arrears problems at the appropriate time.

I. INTRODUCTION

1. During the last seven years, the authorities have maintained close cooperation with the Fund as evidenced by good performance on successive Staff-Monitored Programs (SMPs) and by making payments in excess of obligations falling due. During January 27–February 9, 2006, a staff team visited Khartoum to conduct discussions on the 2006 Article IV consultation, the performance under the 2005 SMP, and an SMP for 2006.¹ The attached Memorandum of Economic and Financial Policies (MEFP, Attachment I) describes the authorities' program and their policy commitments through December 2006.

2. In concluding the last Article IV consultation on April 29, 2005, Directors stressed the importance of keeping inflation low, strengthening the tax base, improving oil sector transparency, and containing nonconcessional borrowing. During the midyear review of the SMP on December 2, 2005, Directors urged the authorities to press ahead with the implementation of the Comprehensive Peace Agreement (CPA) and redouble efforts to resolve the crisis in Darfur. Directors also encouraged the authorities to formulate a prudent budget for 2006, scale back fuel subsidies, adopt the Government Finance Statistics (GFS) methodology, and increase the level of payments to the Fund.²

3. The authorities have been carrying out staff recommendations, although there have been some slippages and delays. Inflation pressures have been contained, and measures to broaden the tax base and improve administration have been undertaken. However, the adoption of GFS (GFSM 2001) methodology has progressed slowly, and the target on nonconcessional borrowing has been missed. The program for 2006 contains important commitments to increase fiscal and oil sector transparency as well as higher payments to the Fund.

4. The framework for assistance to Sudan by donors and multilateral institutions is based on the reports prepared by the Joint Assessment Mission (IMF, UN, World Bank, and the authorities) in early 2005 and the commitments made by donors and the government at the Oslo Conference in April of that year.³ Since then, the first semiannual consultative group meeting (the "Sudan Consortium") to follow up on these commitments, redefine priorities, and foster mutual accountability was held in Paris during March 9–10, 2006 (Appendix II). Fund staff provided input and participated at these events.

¹ The staff team comprised Mr. Gelbard (head), Mr. Ilahi, Mr. Al-Ghelaiah, Ms. Maseeh (all MCD), Mr. Hussain (PDR) and Mr. Chua (FAD). Mr. Pérez (MCD) joined the mission for a few days. Mr. de Schaetzen (Resident Representative) assisted the mission and participated in the discussions. The mission met with senior government officials including the First Vice-President, Mr. Salva Kiir Mayardit; representatives of the business and the banking community; and members of the donor community.

² Most Directors supported the view that the policy commitments under the SMP continued to be in line with what would be required for a Rights Accumulation Program (RAP) and that performance under successive SMPs since 2000 should be taken into account in determining the length of a RAP. A number of Directors suggested that, at the appropriate time, the requirement of a RAP could be waived altogether.

³ The Joint Assessment Mission report to the Oslo Donor Conference in April 2005 provided a comprehensive view of development challenges in Sudan and outlined the areas in need of donor assistance. At that time, donors pledged US\$2 billion in development assistance to Sudan during 2005–07.

II. STOCKTAKING OF PERFORMANCE AND MEDIUM-TERM OUTLOOK

5. Sudan's economic performance in recent years has been good despite adverse security conditions and the difficulties of concluding and implementing the CPA. Growth has been robust, inflation has been at single-digit levels, and important reforms were undertaken. The authorities attained macroeconomic stability, lifted price controls, set up liberal foreign investment and foreign exchange regimes, pursued an ambitious privatization and enterprise-restructuring program, and began a second phase of reforms to liberalize the trade regime. The authorities have also finalized a strategy to try to attain the Millennium Development Goals, increased pro-poor and investment spending in 2005, and plan to finalize an interim Poverty Eradication Strategy in 2006.

6. Notwithstanding these achievements, progress was not smooth and major challenges remain. In the period ahead, Sudan's main tests are to make the Government of National Unity fully operational, achieve peace throughout the country, sustain growth and economic stability, and reduce poverty. The difficulties in ensuring the effectiveness of the new government (and the newly created North-South commissions) cannot be underestimated. Similarly, resolving the crisis in Darfur and dealing with potential unrest in the Eastern provinces is a major challenge. Sustaining growth and stability and fostering poverty reduction will require further structural reforms and addressing the country's social and reconstruction needs. Lastly, the ongoing process of fiscal decentralization requires improvements in implementation capacity, transparency, and coordination at different levels of government.

7. Sudan's economic prospects are promising, but there are also risks. The medium-term outlook, based on the continuation of reform policies, envisages growth of 8–10 percent per year, low inflation, and rising international reserves (Table 1). The economic growth assumptions reflect the effects of the ongoing investment boom, the improved prospects for the South in the period after the peace agreement, and prospective economic reforms. The external current account deficit is projected to decline gradually and remain financed by external capital inflows. Fiscal and balance of payments gaps of about 1.5–2 percent of GDP per year are assumed to be covered by official grants. While the outlook is favorable, there are risks arising from the influence of anti-reform groups that may oppose necessary reforms, unresolved domestic political tensions, and weak institutions (especially at the subnational level).

Sudan: Medium-Term Prospects, 2005–10				
	2005	2006	2007	2008-10 (Average)
	Est.	Projections		
	(Percent of GDP, unless otherwise indicated)			
Real GDP Growth (in percent)	8.0	13.0	10.3	8.9
Oil	-0.2	71.0	28.2	9.0
Non-oil	8.9	7.2	7.5	8.8
Inflation (period average)	8.5	7.5	5.0	3.3
Gross investment	23.3	25.3	26.9	27.4
Fiscal balance	-1.8	-0.9	-0.4	-0.1
Current account balance	-8.5	-5.2	-4.0	-3.7
Crude oil export price (U.S. dollars per barrel)	49.7	47.4	47.2	46.2
Crude oil production (in millions of barrels/day)	0.29	0.49	0.63	0.77

Sources: Sudanese authorities; and Fund staff estimates and projections.

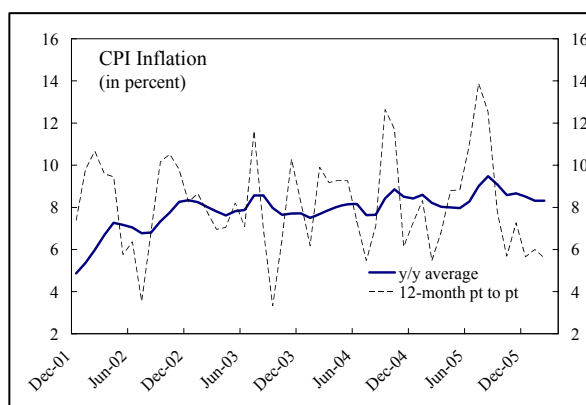
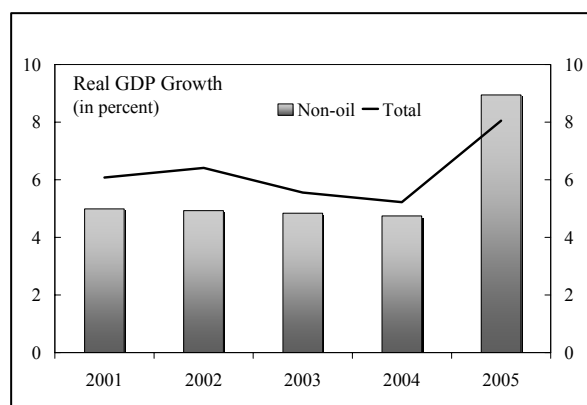
Sources: Sudanese authorities; and Fund staff estimates and projections.

III. RECENT DEVELOPMENTS AND PERFORMANCE UNDER THE PROGRAM

8. **The CPA is being implemented, albeit with some delays.** An interim national constitution was put into force and the Government of National Unity and the government of Southern Sudan were set up in mid-2005.⁴ The central government has begun transferring oil revenues to the South as stipulated in the CPA, although the exact amounts due are still under discussion.⁵ Furthermore, important commissions dealing with North-South borders, the oil sector, and financial aspects of fiscal federalism are not yet functioning effectively.

9. **Progress has been made at the Darfur peace talks in Abuja, but the situation on the ground remains precarious.** There has been progress on a revenue sharing agreement as well as on power-sharing and security arrangements. However, the security situation in Darfur has deteriorated during the last year, and the international community has stepped up pressure for strengthening peacekeeping operations in the region. Relations between Sudan and Chad have also deteriorated because of allegations that each country is supporting rebel forces in the other country.

10. **The economy has been growing at a fast pace and macroeconomic conditions have been stable.** Real GDP grew at an estimated rate of 8 percent in 2005, owing mainly to a recovery in agriculture and robust activity in construction and services. After rapid growth in 2003 and 2004, oil sector output remained virtually unchanged in 2005 at 287 thousand barrels per day (Table 2). Average inflation in 2005 was contained at 8.5 percent. At end-February 2006, the 12-month rate of inflation was 5.8 percent.

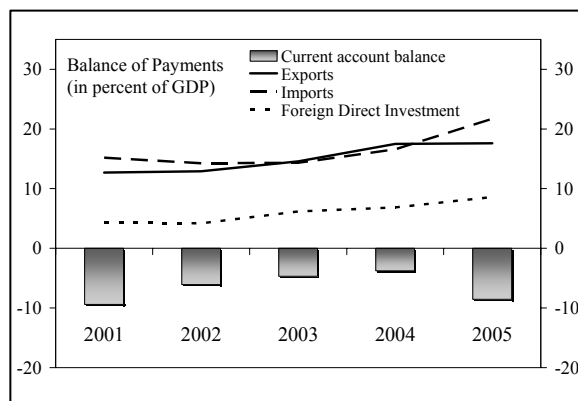


11. **The external current account worsened in 2005, but the balance of payments was supported by strong capital inflows.** Oil export revenues rose because of higher oil prices, but imports rose drastically and non-oil exports slowed. The latter suffered from transportation bottlenecks, high domestic demand, and, possibly, real exchange rate

⁴ Under the new constitution, the national unity government has authority over national sovereignty, central banking, and selected central government functions. The Government of Southern Sudan has a large degree of autonomy (especially on fiscal matters) and responsibility for 10 states in the South.

⁵ The South's share of revenues is based on oil production from fields in the South. However, the precise demarcation of where all fields lie needs to await the work of a technical commission envisaged under the CPA.

appreciation (Box 1). At the same time, the strong trend in capital inflows continued (mainly in the form of foreign direct investment in industrial, telecommunications, transport, and banking activities) allowing for a buildup of net international reserves from 1.9 months of imports at end-2004 to 2.6 months at end-2005 (Table 3).



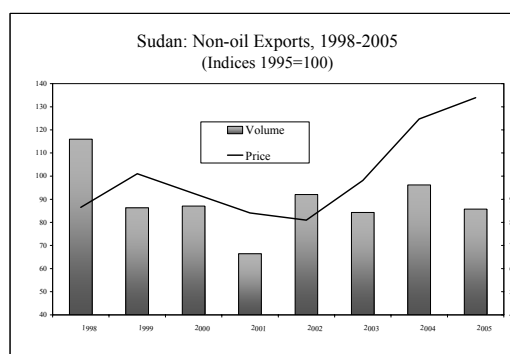
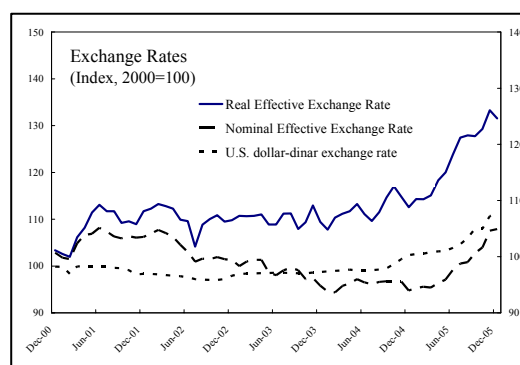
Box 1: Exchange Rate Trends and Competitiveness

Since late 2004, improved market fundamentals coupled with a move towards a market-driven exchange rate have led to an appreciation of the dinar. In 2005, the economy grew at fast pace and higher oil prices led to a 35 percent increase in oil exports. In addition, foreign direct investment rose sharply from US\$1.8 billion in 2003 to US\$3.8 billion in 2005. During the last year, the currency appreciated by 12 percent and 17 percent in nominal and real effective terms, respectively.

Beyond the effects of growth and foreign exchange inflows, higher levels of government spending have also put pressure on nontraded goods' prices and contributed to the real appreciation. Prices of nontraded goods (housing, water, and electricity) grew at an average rate of 11 percent in 2004–05, while prices of tradable goods (food, clothing, and other consumer goods) grew by an average of 6 percent.

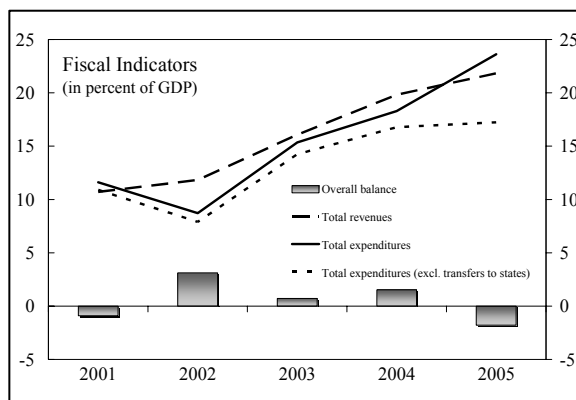
Trade performance also suggests that competitiveness may be deteriorating, although other factors have also played a role. In 2005, the volume of non-oil exports (mainly agricultural products and livestock) fell. Export volumes were also affected by supply constraints (inadequate capacity at the port, deterioration in the road infrastructure), conflict in livestock-rich areas, and higher domestic demand.

Looking ahead, the oil sector boom coupled with strong fundamentals will likely exert further upward pressure on the equilibrium real exchange rate. This highlights the importance of removing structural bottlenecks and improving the business environment to preserve competitiveness in non-oil export and import-competing sectors.



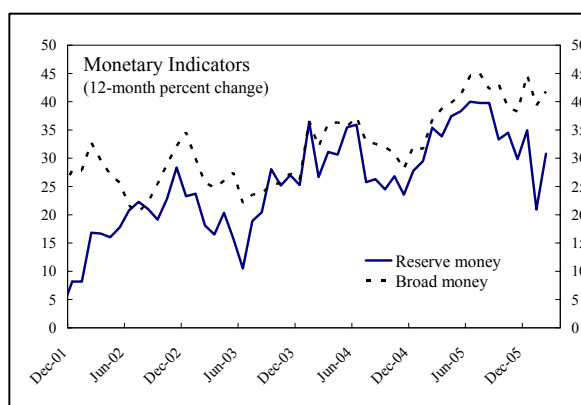
12. After three years of surpluses, the fiscal balance turned into a deficit in 2005.

Oil revenue continued to rise, but it could not keep pace with the increase in government spending (Table 4). Transfers to the South and northern states increased significantly because of the CPA and fiscal decentralization in the North. At the same time, a domestic fuel subsidy equivalent to 3.5 percent of GDP emerged as domestic fuel prices were not increased in line with rising international prices.⁶ The fiscal deficit was financed by bond sales to the domestic nonbank sector and a lower-than-programmed accumulation of deposits in the oil savings account.



13. In 2005, money demand remained high and the dinar appreciated. Money

demand was bolstered by the strong pace of economic activity and increased financial intermediation. Despite central bank's attempts to mop liquidity through open market sales of government securities and foreign exchange, broad money and reserve money grew by 45 percent and 35 percent, respectively (Tables 5 and 6). Credit to the private sector also grew rapidly (by 65 percent) during the year.⁷ Money demand pressures, backed by strong foreign exchange inflows, translated into dinar appreciation.



14. Faced with a trade-off between higher inflation and exchange rate appreciation, the authorities have appropriately allowed the exchange rate to appreciate. In the context of Sudan's managed floating exchange rate regime, the authorities have been monitoring inflation developments closely and allowed the exchange rate to appreciate in response to incipient inflationary pressures. While also aimed at containing excessive exchange rate volatility, foreign exchange market intervention has been geared to the attainment of the program's foreign exchange accumulation reserves objectives rather than targeting an implicit path for the exchange rate.

⁶ Fuel prices are set administratively and the estimated fuel subsidies are implicit; that is, they reflect domestic sales at below export prices with no explicit compensation in the budget. The staff has urged the authorities to record these subsidies as an explicit expenditure item and set an automatic adjustment mechanism to adjust them in line with world prices.

⁷ About 60 percent of the new credit was channeled to the services and trade sectors. Regarding the concentration of the new credit, almost 40 percent originated in a single bank. The central bank has stepped up supervision of this bank to monitor its lending portfolio.

15. **The authorities took steps to improve the import tariff structure and increase flexibility in the foreign exchange market.** As part of a three-year import-tariff reform program, the authorities lowered the top tariff rate from 45 percent to 40 percent. The average tariff fell to 20 percent, and there are plans to reduce it further to 15 percent or less by 2008 (MEFP, ¶23). Regarding the foreign exchange market, the authorities have recently allowed for further flexibility (through auctions) in the pricing of foreign exchange. Sudan maintains an exchange system free of restrictions on the making of payments and transfers for current international transactions (Appendix I).

16. **Banking system soundness indicators improved in 2005.** The ratio of nonperforming loans to total loans fell from 8.9 percent in 2004 to 6.9 percent at end-2005. During the same period, capital adequacy ratio for the banking system increased from 10.8 percent to 12 percent (Table 5).⁸

17. **The authorities made progress with the envisaged fiscal and financial sector reforms.** They set up a medium taxpayer unit to boost non-oil revenue collection, adopted the Automated System for Customs Data at customs ports, and strengthened cash management through cash plans and better coordination between the ministry of finance and the central bank. Regarding monetary and financial sector reforms, the central bank introduced competitive auctions of government securities, implemented a new financing window for banks using collateral-based certificates, and privatized a large bank (Khartoum Bank). The authorities have also been setting up the new federal structure in the banking system (required by the CPA) by enacting laws to restructure the central bank and banking activities and by establishing a branch of the central bank in the South. Furthermore, the central bank has formulated a strategy for screening mergers and acquisitions and opened the banking sector to foreign banks.⁹

18. **Performance under the 2005 SMP was broadly satisfactory.** Three of the five quantitative targets and all but one structural benchmark for end-December 2005 were met (Tables 7 and 8). The target on the domestic financing of the fiscal deficit was missed by a small margin, while the ceiling on nonconcessional borrowing was not observed as US\$935 million in loans were contracted during the year. The authorities explained that, in the absence of concessional financing, these loans financed key water and electricity projects.¹⁰ The structural benchmark on converting the 2006 budget in GFSM 2001 format was delayed because of technical difficulties in the preparation of the budget; the authorities expect to implement this measure in May 2006.

⁸It should be noted that measures of regulatory capital in Sudan are artificially high because fixed assets are improperly counted as capital. The authorities are reviewing accounting norms for commercial banks to correct the problem.

⁹ In 2005, the authorities granted four licenses for new banks.

¹⁰ Project-related nonconcessional loan contracts with China amounted to US\$814 million, while contracts with the Islamic Development Bank and the Arab Monetary Fund amounted to US\$102 million. Iran provided a loan for US\$19 million with a grant element of 25 percent.

IV. REPORT ON THE DISCUSSIONS

19. The discussions focused on economic policies for 2006 and macro-relevant structural measures to sustain growth and foster poverty reduction, and the 2006 SMP. The main Article IV issues relate to the need to consolidate macroeconomic stability and pursue pending reforms. In this context, particular attention was given to the need to streamline tax exemptions, create the conditions for successful fiscal decentralization, improve efficiency and transparency in public sector operations, and support continued private sector development in light of the recent appreciation of the dinar. The program for 2006 contains measures to maintain inflation in single-digits, keep the fiscal deficit under control, reorient public spending to increase pro-poor outlays and reduce fuel subsidies, and implement key measures to improve fiscal and oil-sector transparency and reform the financial sector.

A. Macroeconomic Policies

20. **The economic outlook for 2006, underpinned by higher oil output, is favorable.** The macroeconomic framework envisages GDP growth of 13 percent and average inflation of 7.5 percent. The non-oil sector is expected to grow by 7 percent, but oil production will increase by nearly 70 percent (to 492,000 barrels per day) as two new oil fields come on stream. The new oil (Dar blend) is of lower quality compared to Sudan's traditional oil (Nile blend). The forecast for 2006 envisages prices of US\$55 and US\$40 per barrel of Nile blend and Dar blend, respectively.

21. **The fiscal stance in 2006 is intended to support macroeconomic stability.** The overall fiscal deficit is projected to fall from 1.8 percent in 2005 to 0.9 percent of GDP in 2006 because of higher oil revenues.¹¹ The domestic financing of the deficit is expected to be 0.3 percent of GDP (compared to 1.6 percent in 2005) and is consistent with a financial program that targets 7.5 percent inflation and a further accumulation of international reserves.¹²

22. **The authorities intend to reinvigorate the non-oil revenue effort of recent years and to continue saving resources in the oil savings account.** Oil revenues will rise because of higher

Sudan: Selected Fiscal Indicators, 2004–06			
	2004	2005 Est.	2006 Prog.
(In percent of GDP)			
Total revenue	19.8	21.8	24.0
Of which: Oil	10.4	13.4	14.3
Total expenditure	18.3	23.6	24.9
Of which: Fuel subsidies	0.0	3.5	1.8
Transfers to the South	0.4	2.8	4.0
Transfers to other states	1.1	3.6	4.2
Overall balance	1.5	-1.8	-0.9
Memorandum items:			
Consolidated capital spending	5.0	5.5	6.9
Pro-poor spending	...	2.8	5.1
Sources: Sudanese authorities; and IMF staff estimates and projections.			

¹¹ The fiscal framework is based on revised oil revenue and expenditure projections compared to the original 2006 budget. The authorities intend to inform Parliament about the changes to the original budget as mentioned in the MEFP.

¹² Given the potential for crowding out associated with high domestic borrowing, the authorities' program envisages a decline in borrowing from the nonbank sector from 1.3 percent of GDP in 2005 to 0.7 percent of GDP in 2006.

oil output, while non-oil revenues are expected to increase because of improvements in administration (including tax collection in the South) and a rationalization of tax exemptions (see Section B below). The oil savings account is expected to accumulate the equivalent of 1.4 percentage points of GDP in 2006.

23. **Given the need to preserve macroeconomic stability, the authorities' fiscal framework for 2006 envisages a reorientation of expenditures away from lower priority areas.** The fiscal framework envisages a moderate growth in outlays on wages and on goods and services and a smaller fuel subsidy.¹³ The authorities recognize that the fuel subsidy does not benefit the poor and, despite opposition from vested interest groups, intend to begin dealing with the problem in 2006. They consider that a large increase in fuel prices could be counterproductive, but will be informing the public about the costs of the subsidy and developing a strategy for the automatic pass-through of changes in world prices in the future.¹⁴

24. **The authorities' plan to devolve resources to the states and foster national unity through infrastructure investments entails a sizable increase in public spending.** Central government transfers to the South and to northern states are expected to grow significantly in 2006. The bulk of the latter (meant for state-level spending on health, education, and water) and some national capital expenditures are deemed pro-poor.¹⁵ The authorities recognize that capacity constraints will condition the effectiveness of such spending, but see their strategy as the only option to reduce poverty in disadvantaged areas and prevent the disintegration of the country.

25. **Successful decentralization will require good budget preparation procedures, sound budgetary and financial management, transparency, and effective monitoring.** Careful coordination of expenditure and borrowing plans between the Government of Southern Sudan, the northern states, and the central government will be critical in safeguarding macroeconomic stability. The newly created Fiscal and Financial Allocation and Monitoring Commission (FFAMC) established under the CPA will need to lead and coordinate work in these areas.

26. **The authorities plan to focus on attaining reserve money targets in an environment of exchange rate flexibility.** Reserve and broad money growth are targeted at 25 percent and 28 percent, respectively, consistent with the GDP growth and inflation objectives and with an increase in money demand driven by financial deepening and the reintegration of the South. The conduct of monetary policy will require the flexible use of

¹³ While some fuels are priced close to international levels, selected fuels such as gas oil carry a large subsidy element. Sudan's level of (implicit) fuel subsidies in 2005 (3.5 percent of GDP) was in the middle range compared to other oil exporters. The staff estimates that a price increase of 60 percent will be needed to eliminate the subsidy on gas oil.

¹⁴ The decline in the fuel subsidy in 2006 reflects, in part, a decline in fuel imports that enjoy a higher subsidy per unit compensated by a significant increase in the domestic production of such products. The subsidy is also lower because of the recent appreciation of the dinar and lower oil prices in 2006.

¹⁵ The aggregate level of pro-poor spending in 2006 is close to the more than doubling of such spending (in percent of GDP) promised by the government at the Oslo Donors' Conference in 2005.

instruments (e.g. domestic open market operations and foreign exchange market operations) to deal with a number of uncertainties such as the fiscal behavior of subnational governments, money demand in the South, and foreign exchange inflows. While the authorities expressed concern about exchange rate appreciation pressures and external competitiveness, they agreed with the staff that maintaining flexibility in the exchange rate combined with improvements in the business environment through structural reforms is the most appropriate policy response. In this regard, they intend to carry out a World Bank-sponsored investment climate assessment later this year.

B. Structural Reforms

27. The authorities agreed on the need to reinvigorate the reform momentum by proceeding with the implementation of pending reforms. The discussions covered selected reforms in the following areas: tax policy and administration, expenditure management, oil sector transparency, and financial system restructuring.

28. **Tax policy and administration.** Following efforts over the last few years to streamline exemptions and improve administration, the authorities recognize the need to reinvigorate reforms in these areas (Box 2). As part of the program, they intend to stop the renewal of expired business-profits tax and customs-duty exemptions, introduce self-assessment for large and medium-sized taxpayers, and set up three federal tax offices in major cities in the South. The authorities also intend to prepare a program to revamp the system of investment incentives in line with best international practices.

Box 2: Tax Reforms—Progress and Future Agenda

Sudan has carried out important tax policy and administration reforms in recent years. The main policy reforms were the introduction of a value-added tax, the phasing out of privileges for major oil distribution companies, and the removal of income tax exemptions. Key administration reforms involved setting up large and medium taxpayer units, enforcing departmental fee collection, and implementing the Automated System for Customs Data. Because of these reforms, non-oil tax revenues as a share of non-oil GDP rose from 7 percent in 2002 to 9.9 percent in 2005.

Notwithstanding these achievements, further reforms are needed:

- The Investment Encouragement Act should be modified by removing tax holidays and customs duty exemptions while grandfathering existing beneficiaries. To improve the cost-effectiveness of investment promotion, a system of accelerated depreciation should be implemented.
- A low (20 percent or less) uniform business profit tax (currently, there are different rates depending on the type of economic activity) needs to be adopted.
- VAT exemptions, especially on capital goods and selected consumer goods need to be scaled back.
- Improve audit and collection enforcement by the large taxpayers unit and implement self-assessments by taxpayers and risk-based methods in tax and customs administration.

29. **Expenditure management.** The authorities recognize that the success of the rapid move to a decentralized system of public finances depends on appropriate regulations, implementation capacity, transparent reporting, and effective monitoring mechanisms. At present, however, capacity in the South and other states is weaker than at the central government, highlighting the need for urgent investments in administration and training. A key initial step is to ensure the efficient operations of the new Fiscal and Financial Allocation and Monitoring Commission (FFAMC). At the same time, close cooperation between the federal government, the Government of Southern Sudan, and other state governments will be essential to coordinate development planning and implementation and attain good macroeconomic outcomes (Box 3). Regarding fiscal reporting, the authorities intend to pursue an ambitious timetable for compiling budget execution reports according to the GFSM 2001 format (covering operations of the central government and the government of Southern Sudan). Lastly, the government is conducting its first public expenditure review in consultation with the World Bank (Fund staff will assist on revenue management).

Box 3: Macroeconomic Challenges of Implementing the CPA

The CPA contains numerous peace-related provisions (including the modalities of power and wealth sharing with the South) and strengthens the federal system of government in Sudan. On the monetary front, the CPA envisages a new national currency and a single monetary policy conducted from Khartoum. On fiscal matters, the CPA confers autonomy to the South by transferring a share of national oil revenues and allowing the South to levy state taxes and retain one-half of the federal taxes collected in the region. The Government of Southern Sudan and other states can also borrow at home or abroad.

The challenges of implementation and the implications for macroeconomic outcomes are manifold:

- *Monetary policy.* The central bank plans to introduce conventional instruments of monetary policy in the South because of the dual nature of the new banking system stipulated in the CPA (Islamic banking in the north and conventional banking in the South). The central bank will also need to strengthen its regulatory and supervisory capacity to cover banks in the South.
- *Single currency.* Introducing a new currency is essential to provide for a single means of payments in the South, develop its economy, and integrate the South with the rest of the country.
- *Tax collection.* The Government of Southern Sudan lacks capacity and infrastructure to collect taxes in its territory. Customs posts and tax offices will gradually begin to operate this year.
- *Coordination of spending.* Coordinating the composition of expenditures will be essential to ensure the harmonization between national projects and those in the South and allow the central government to formulate a countrywide public expenditure program. Coordinating the timing of expenditures is also crucial to ensure a smooth conduct of monetary policy.
- *Transparency and monitoring.* The FFAMC will be critical to ensure transparency and monitor the allocation of nationally collected funds to the Government of Southern Sudan and northern states.
- *Coordination on budget preparation and execution.* Coordination on budget preparation and execution (including coordination of borrowing plans) will be necessary to safeguard fiscal sustainability and macroeconomic stability.

30. **Oil sector transparency.** The authorities' near-term reforms in this area include the monthly publication of detailed oil sector data, the completion and publishing of the audit of Sudapet (a state-owned oil company with equity stakes in a number of fields), and the regularization of the hitherto ad hoc transfers of profits from the state-owned oil companies to the treasury (MEFP, ¶21). The authorities are also expected to clarify the operational role of the National Petroleum Commission, a high-level body created under the CPA to manage oil sector policy.

31. **Financial system restructuring.** Cognizant of the importance of implementing CPA-related financial sector reforms, the authorities intend to proceed with the restructuring of the central bank and the introduction of the new currency. MFD has been providing intensive technical assistance in these areas. The most critical reform is the introduction of the new currency, and the authorities are aware of the risks involved, i.e., inappropriate planning for distribution and lack of safeguards to prevent fraud at the time of implementing the currency exchange. Following on the Financial System Stability Assessment (FSSA) prepared in March 2005, the authorities are also proceeding with a strategy to restructure commercial banks based on increasing minimum capital requirements and capital adequacy ratios and ensuring banks' compliance with prudential norms.

C. External Debt and Relations with Creditors

32. **Sudan's debt overhang continues to condition development prospects.** At end-2005, the stock of public and publicly guaranteed external debt was US\$27.7 billion, of which US\$24.4 billion was in arrears.¹⁶ In present value terms, the estimated stock of debt is US\$26 billion, or about 690 percent of the three-year average of exports of goods and services. The authorities are worried that, after seven years of successful implementation of consecutive SMPs, Sudan's pressing needs to finance programs for achieving the Millennium Development Goals cannot be met because of lack of access to concessional resources related to Sudan's debt problems.

33. **To strengthen Sudan's record of cooperation with the Fund, the authorities committed to increase the level of payments to the Fund to US\$45 million in 2006.** In recent years, Sudan's payments to the Fund have exceeded obligations falling due, leading to a small decline in arrears. In 2005, Sudan paid US\$30 million to the Fund as envisaged under the SMP. The staff emphasized the importance of increasing payments to the Fund in light of the deterioration of a number of indicators showing payments as a share of debt service capacity (Table 9). The authorities have taken this decision notwithstanding the need to deliver a peace dividend and a reduction in the fiscal space because of the requirements of the CPA.¹⁷

¹⁶ About 70 percent of the debt is owed to official bilateral creditors (almost equally divided between Paris Club and non-Paris Club creditors). The remaining debt is owed to multilateral institutions (17 percent) and commercial creditors (13 percent).

¹⁷ As shown in Table 9, the increase in payments has begun to reverse the erosion of Sudan's payments to the Fund in relation to various indicators of debt service capacity, including official reserves.

34. **Sudan has been making debt service payments to almost all multilateral creditors and selected bilateral creditors that have provided new financing in recent years.** In 2005, multilateral creditors excluding the IMF, World Bank, and the African Development Bank made a net resource transfer of US\$74 million, while Arab bilateral creditors made a net transfer of US\$68 million. In the same year, Sudan paid other bilateral creditors (China, India, and Malaysia) a net amount of US\$84 million. These creditors have financed a number of water and electricity projects in recent years (IMF Country Report No.05/180).

35. **The staff urged the authorities to minimize nonconcessional borrowing,** noting the potential complications with a potential debt relief operation and the higher cost of debt relief for existing creditors. The authorities emphasized that their strategy to foster national unity called for undertaking substantial investment projects and that, in light of the limited fiscal space after the peace agreement and lack of access to concessional financing, they had to finance these projects from other sources. They also noted that these loans should be viewed as exceptional and that they are project-specific facilities to be disbursed over a number of years, not direct budget support. Lastly, the authorities expressed concern that it may take a long time until sanctions are removed and Sudan can regularize its debt situation. The authorities' initial borrowing plans for 2006 amounted to US\$1.1 billion. The staff pressed the authorities to prioritize their projects and minimize this type of borrowing. The authorities later indicated that they could limit this type of borrowing to about US\$700 million. Almost two-thirds of the borrowing would be for projects related to the reconstruction of a North-South railway and the construction of roads to the South and to Darfur.¹⁸ The authorities acknowledged the concern of Sudan's creditors about this borrowing, and committed to limit contracting these facilities as much as possible, especially if concessional financing becomes available.

D. Data Issues and Technical Assistance

36. **Sudan's economic data is sufficient for surveillance and program monitoring, but inadequacies remain.** The quality of Sudan's economic data has improved in recent years, especially through the participation in the Fund's General Data Dissemination System. Monetary and financial sector statistics are comprehensive and timely, and detailed data on oil sector shipments, revenues, and payments are available regularly. However, fiscal expenditure data are not compatible with GFS methodology, national accounts are virtually nonexistent, details on oil production from new blocks are not available, and statistics on capital goods imports and foreign direct investment are weak.

37. **In the near term, Sudan's technical assistance priorities** comprise the adoption of GFSM 2001 methodology (budget classification, accounting, auditing, and reporting); tax administration; fiscal decentralization and public financial management; issuance of the new currency; banking supervision and liquidity management; and fiscal and real sector statistics. The Fund is coordinating a technical assistance program on financial sector reforms and is

¹⁸ The remaining amount is intended for water and irrigation projects. The authorities noted that these intentions are plans and not final operations. They indicated that they would seek to obtain the highest possible degree of concessionality and will not use oil as collateral. These potential loans are not yet factored in the fiscal or the balance of payments projections.

expected to continue providing assistance on some of the fiscal areas mentioned above. In addition, with occasional support from Fund staff, the World Bank will continue providing technical assistance to the Government of Southern Sudan on several areas including public financial management.

E. The 2006 Staff-Monitored Program

38. **The program for 2006 aims at maintaining macroeconomic stability, ensuring the implementation of macro-relevant commitments under the CPA, and increasing fiscal and oil sector transparency.** The macroeconomic objectives and the policy commitments are described in the MEFP and were mentioned in sections A-C above. The program contains measures to keep inflation at no more than 7.5 percent, increase budget allocations on social and infrastructure projects, and lower the fuel subsidy. Other commitments include establishing rules and procedures for the FFAMC, beginning fiscal reporting according to GFS, publishing detailed oil sector data and oil-related transfers to the South, and introducing the new national currency.

V. RISKS TO THE OUTLOOK

39. Sudan's economic prospects are good, but significant risks exist. The main risk is a weakening of political resolve to maintain macroeconomic stability, advance critical reforms, and foster Sudan's integration with the world economy. This could set off a negative cycle of bad policies and worsening prospects for a united and peaceful Sudan. At the same time, the authorities' hope that Sudan's good performance under successive SMPs over the past seven years would pave the way for a resolution of Sudan's debt problems has not yet materialized. While the authorities want to foster Sudan's integration with the world economy and are aware of the negative impact of developments in Darfur on the views of key creditor countries, they are also concerned that the persistence of the external arrears problems and the lack of concessional financing may make it more difficult to continue implementing the reform agenda.

40. The lack of resolve could manifest itself in delayed action to lower fuel subsidies and implement fiscal and oil-sector transparency reforms as well as an inability to adhere to the fiscal spending ceilings. There are also potential pitfalls in trying to mount a modern administration in the South and in other states, prevent wasteful spending of transfers to subnational governments, and carry out a successful monetary policy amidst unpredictable spending patterns of subnational governments.

VI. STAFF APPRAISAL

41. Despite a difficult year marked by the beginning of the implementation of the CPA and a deterioration of the security situation in Darfur, the authorities managed to strike a balance between the pressures for a peace dividend and policies that maintained macroeconomic stability. Economic growth in the non-oil sector was robust, foreign direct investment reached new heights, and inflation was contained within single-digit levels. While there were some slippages on budget execution (mainly because of the fuel subsidy) and a higher-than-projected level of nonconcessional borrowing, most of the quantitative and structural targets under the program were met. As a result, performance under the 2005 SMP was broadly satisfactory. Since some policy actions were delayed last year, the authorities will need to press ahead with those policies and other critical reforms to achieve their objectives.

42. The program for 2006 aims at sustaining Sudan's recent record of high growth, preserving macroeconomic stability, and meeting the country's development and poverty reduction needs. The program contains a prudent fiscal framework with realistic revenue and expenditure assumptions, as well as a reorientation of public spending toward social and infrastructure investments. The staff is particularly encouraged by the authorities' commitment to improve fiscal and oil sector transparency. However, the continued reliance on nonconcessional borrowing is a serious concern.

43. Despite an increase in oil revenues in 2005–06, the fiscal space of the central government has been constrained because of the sizable increase in transfers required by the peace agreement and decentralization. The increase in transfers, coupled with higher capital expenditures, will lead to a substantial increase in pro-poor development spending. At the same time, the authorities will need to focus on improving expenditure management and monitor closely the effectiveness of the additional spending. In this context, the intended reorientation of public spending is welcome, including the much-needed steps to reduce fuel subsidies. Regarding the latter, the staff urges the authorities to bring domestic fuel prices in line with export prices and develop an automatic mechanism for future price adjustments.

44. The staff urges the authorities to press ahead with the fiscal reform priorities. These include rationalizing investment incentives to protect the non-oil tax revenues; building capacity, transparency, and accountability at all levels of government to support decentralization; and improving fiscal transparency through the adoption of GFS methodology. The authorities also need to redouble their efforts to ensure close coordination between the Government of Southern Sudan, the northern states, and the central government.

45. Monetary policy should continue to focus on attaining the authorities' inflation objectives in an environment of exchange rate flexibility. Fiscal prudence and a proactive monetary policy with close management of reserve money will help to ensure that inflation remains subdued. The authorities will also need to ensure flexibility in the pricing of foreign exchange to prevent the excessive monetization of external inflows and thus accommodate a prospective real exchange rate appreciation without rekindling inflationary pressures. In this regard, the current managed floating exchange rate regime remains appropriate. At the same time, structural reforms to remove structural rigidities and lower transactions costs will be

the best way to safeguard external competitiveness and improve profitability in non-oil exports and import-competing sectors.

46. The authorities should be commended for the implementation of a number of financial system provisions of the CPA. In 2006, the central bank will need to proceed with its internal restructuring, provide the basis for the effective functioning of a dual banking system, and introduce the new currency. The staff urges the authorities to embark on a well-planned, expeditious, and transparent process to introduce the new currency given the importance of the latter in fostering development in the South and the country's economic integration.

47. Sudan's external debt problems continue to constrain access to external development financing. Sudan's record of cooperation on economic policies and payments to the Fund in recent years augur well for the clearance of Sudan's arrears at the appropriate time. In the meantime, the authorities' should strive to minimize contracting nonconcessional debt as such borrowing threatens debt sustainability and could delay the process of securing creditors' participation in a potential debt-relief operation. In this regard, the staff underscores that it will be critical for creditors and Sudan to treat all such new borrowing under the Highly Indebted Poor Countries' Initiative. This will ensure that any eventual relief provided under the Initiative is sufficient to restore debt sustainability.

48. Looking ahead, the authorities should focus on the implementation of the CPA, sustained efforts to achieve peace throughout the country, capacity building, and the effective use of Sudan's oil wealth. In the near term, the main risk is a weakening of the reform effort. In this regard, the authorities should also strive to preserve macroeconomic stability and proceed with the reforms envisaged in the 2006 program. These include conducting a prudent monetary policy in a flexible exchange rate environment, adhering to the fiscal spending targets, monitoring the effectiveness of public spending, lowering fuel subsidies, and proceeding with the envisaged fiscal and oil-sector reforms.

49. While the proposed level of nonconcessional borrowing implies that in this area the program is no longer equivalent to an upper-credit tranche arrangement, the SMP is a valuable tool to support the reform momentum at a critical juncture in the country's history when the CPA needs to be implemented amidst a complex political environment. The program contains important actions to preserve economic stability and increase fiscal and oil-sector transparency as well as higher payments to the Fund. It also provides a framework within which donors can support the peace process and afflicted areas. Except for the high level of nonconcessional borrowing, the staff considers that the 2006 SMP continues to be equivalent in strength to a Rights Accumulation Program.

50. Sudan's economic data remains generally adequate for surveillance and program monitoring. It is proposed that the next Article IV consultation with Sudan be held according to the standard 12-month cycle.

Table 1. Sudan: Medium-Term Macroeconomic Scenario, 2005–10

	2005 Est.	2006	2007	2008	2009	2010
		Projections				
(Change in percent, unless otherwise indicated)						
Production and prices						
Nominal GDP (in millions of U.S. dollars)	27,699	36,030	42,339	47,923	52,913	58,558
Real GDP	8.0	13.0	10.3	9.3	8.7	8.6
Oil	-0.2	71.0	28.2	13.5	7.3	6.2
Non-oil	8.9	7.2	7.5	8.5	9.0	9.1
Inflation (period average)	8.5	7.5	5.0	4.0	3.0	3.0
(In percent of GDP, unless otherwise indicated)						
Investment and saving						
Gross investment	23.3	25.3	26.9	27.7	27.6	27.0
Government 1/	5.5	6.9	8.3	8.7	8.3	8.0
Nongovernment	17.8	18.4	18.6	19.0	19.3	19.0
Gross national saving	14.8	20.1	22.9	24.4	23.4	23.5
Government	3.7	6.1	8.0	8.5	8.1	8.0
Nongovernment	11.1	14.1	14.9	15.9	15.3	15.4
Central government						
Total revenue	21.8	24.0	25.8	27.5	27.1	27.7
Of which: Oil revenue 2/	13.4	14.3	16.4	17.7	17.2	17.5
Total expenditure	23.6	24.9	26.2	27.7	27.3	27.6
Overall balance (cash basis)	-1.8	-0.9	-0.4	-0.2	-0.2	0.0
External sector						
External trade balance	-4.0	1.9	4.4	5.3	3.9	3.2
Exports	17.4	22.0	24.1	24.8	23.0	21.8
Imports	21.5	20.1	19.7	19.5	19.1	18.6
Current account balance on cash basis 3/	-8.5	-5.2	-4.0	-3.4	-4.2	-3.5
Net international reserves (in months of imports)	2.6	3.1	3.5	4.3	4.6	5.1
Non-oil export volume (change in percent)	-12.4	6.5	9.8	11.1	11.4	11.9
Non-oil import volume (change in percent)	55.2	21.0	14.5	11.5	7.6	6.6
Terms of trade (change in percent)	24.4	-4.6	-0.8	-0.2	-3.0	-2.8
Memorandum item:						
Crude oil export price (U.S. dollars per barrel) 4/	49.7	47.4	47.2	47.4	46.1	45.2

Sources: Sudanese authorities; and Fund staff estimates and projections.

1/ Includes estimated capital spending by state governments.

2/ Crude oil revenue.

3/ Includes expected official transfers of about \$1.8 billion pledged in Oslo for the 2006-08 period.

4/ The projections for Sudanese oil blends are based on March 2006 WEO oil prices.

Table 2. Sudan: Selected Economic and Financial Indicators, 2001–06

	2001	2002	2003	2004	2005		2006
					Prog.	Prel.	Proj.
(Annual changes in percent, unless otherwise indicated)							
Production, population, and prices							
Nominal GDP (in billions of Sudanese dinars, at market prices)	3,454	3,978	4,614	5,573	6,912	6,748	8,107
Nominal GDP (in millions of U.S. dollars)	13,369	15,109	17,680	21,610	28,050	27,699	36,030
Crude oil production (in thousands of barrels per day)	209	232	262	288	312	287	492
Population (in millions)	31.9	32.7	33.6	34.5	35.4	35.4	36.3
GNP per capita (in U.S. dollars)	374	425	486	579	790	790	903
Real GDP	6.1	6.4	5.6	5.2	8.2	8.0	13.0
Oil	21.6	24.7	13.0	9.9	8.2	-0.2	71.0
Non-oil	5.0	4.9	4.8	4.7	8.2	8.9	7.2
Consumer prices (average)	4.9	8.3	7.7	8.4	10.5	8.5	7.5
Consumer prices (end of period)	7.4	8.3	8.3	7.3	9.1	5.6	6.0
(In percent of GDP)							
Investment and saving							
Gross investment	17.6	19.4	20.0	22.5	21.9	23.3	25.3
Government 1/	2.3	3.0	2.9	5.0	4.9	5.5	6.9
Nongovernment	15.3	16.4	17.0	17.5	17.8	17.8	18.4
Gross national saving	8.2	13.4	15.3	18.7	16.9	14.8	20.1
Government	1.4	2.2	3.9	6.1	4.7	3.7	6.1
Nongovernment	6.8	11.2	11.4	12.6	12.2	11.1	14.1
Central government operations 2/							
Total revenue	10.7	11.8	16.1	19.8	22.4	21.8	24.0
Total expenditure	11.6	8.7	15.4	18.3	23.0	23.6	24.9
Overall balance (cash)	-0.9	3.1	0.7	1.5	-0.6	-1.8	-0.9
Money and credit							
Broad money (change in percent)	24.7	30.3	30.3	32.1	33.0	44.7	28.0
Reserve money (change in percent)	3.7	22.0	26.6	27.8	29.9	34.9	25.0
Velocity (non-oil nominal GDP over average broad money)	8.1	7.1	6.6	5.7	4.9	4.8	4.2
(In millions of U.S. dollars; unless otherwise indicated)							
External sector							
Exports, f.o.b.	1,699	1,949	2,577	3,778	5,619	4,825	7,936
Of which: Oil	1,377	1,511	2,082	3,101	4,915	4,187	7,226
Imports, f.o.b.	2,031	2,153	2,536	3,586	5,122	5,946	7,248
Non-oil export volume (change in percent)	-22.2	41.3	-6.9	7.8	1.1	-12.4	6.5
Non-oil import volume (change in percent)	31.2	4.8	6.6	27.9	33.4	55.2	21.0
Current account balance (cash basis, percent of GDP)	-9.4	-6.1	-4.7	-3.8	-5.0	-8.5	-5.2
Terms of trade (Index 1993 = 100, change in percent)	-8.6	-2.3	8.9	20.8	27.6	24.4	-4.6
Dinars per U.S. dollar (period average)	258	263	261	258	...	244	...
Real effective exchange rate (change in percent) 3/	8.1	-1.7	-0.5	2.7	...	16.8	...
External debt (in billions of U.S. dollars)	20.9	23.6	25.7	26.0	27.0	27.7	28.8
External debt (percent of GDP)	156.7	156.3	145.4	120.3	96.1	100.0	79.9
Debt service ratio (commitment basis) 4/	39.6	38.3	32.2	23.6	16.8	19.6	12.9
Debt service ratio (cash payments) 4/	5.1	6.8	9.5	7.9	5.8	5.6	4.9
Net international reserves (in millions of U.S. dollars) 3/	-109	84	290	1,144	2,005	1,889	2,589
In months of next year's imports	-0.5	0.3	0.8	1.9	2.9	2.6	3.1
Sudan's crude-oil export price (U.S. dollars per barrel)	22.0	23.0	27.0	36.4	51.8	49.7	47.4

Sources: Sudanese authorities; and Fund staff estimates and projections.

1/ Includes estimated capital spending by state governments.

2/ Cash basis.

3/ End of period.

4/ As a share of exports of goods and services.

Table 3. Sudan: Balance of Payments, 2002–06

	2002	2003	2004	2005		2006
				Rev. Prog.	Prel.	Prog.
(In millions of U.S. dollars, unless otherwise indicated)						
Current account balance	-1,488	-1,369	-1,352	-1,989	-2,954	-2,486
Current account balance (on cash basis)	-918	-827	-816	-1,404	-2,341	-1,874
Trade balance	-204	40	192	497	-1,121	688
Exports, f.o.b.	1,949	2,577	3,778	5,619	4,825	7,936
<i>Of which:</i> Crude oil exports	1,397	1,968	2,962	4,704	3,948	6,867
Petroleum products	114	114	138	211	239	359
Non-oil products	438	494	677	704	638	709
Imports, f.o.b.	-2,153	-2,536	-3,586	-5,122	-5,946	-7,248
Services (net)	-724	-794	-1,020	-1,632	-1,643	-2,187
Income (net)	-1,226	-1,334	-1,647	-2,080	-1,912	-3,276
Receipts	19	10	22	37	44	58
Non-oil payments	-614	-603	-631	-674	-684	-695
Oil related expenses 1/	-631	-740	-1,038	-1,444	-1,271	-2,638
Current transfers (net)	666	718	1,123	1,226	1,721	2,289
<i>Of which:</i> Private transfers (net)	634	708	1,095	1,134	1,487	1,522
Capital account	2	0	0	0	0	0
Financial account (net)	499	1,045	1,194	1,894	2,688	2,390
Disbursements	30	85	191	231	309	395
Amortization	-166	-239	-280	-290	-290	-358
<i>Of which:</i> cash payments	-84	-161	-187	-223	-185	-277
Payments to the Fund	-24	-26	-32	-30	-30	-45
Short-term capital flows (net) 2/	189	138	-140	113	496	96
Net foreign assets of banks (increase -)	-163	-5	-26	-250	-153	-30
Foreign direct investment and portfolio (net)	633	1,092	1,481	2,090	2,355	2,332
Errors and omissions	582	12	272	291	315	0
Overall Balance	-405	-312	114	196	49	-96
Overall Balance (on cash basis)	247	308	743	849	767	597
Change in net international reserves (increase -)	-197	-204	-855	-849	-745	-700
Earmarked reserve assets (increase -)	-90	-125	112	...	-23	103
Exceptional financing	693	642	629	652	719	693
Change in arrears	652	620	629	652	719	693
Privatization receipts	41	22	0	0	0	0
Financing gap	0	0	0	0	0	0
(In percent of GDP, unless otherwise indicated)						
Memorandum items:						
Current account balance (accrual basis)	-9.8	-7.7	-6.3	-7.1	-10.7	-6.9
Current account balance (cash basis)	-6.1	-4.7	-3.8	-5.0	-8.5	-5.2
Current transfers (net)	4.4	4.1	5.2	4.4	6.2	6.4
<i>Of which:</i> Private transfers	4.2	4.0	5.1	4.0	5.4	4.2
Net international reserves (in million of U.S. dollars)	84	290	1,144	2,005	1,889	2,589
In months of next year's imports	0.3	0.8	1.9	2.9	2.6	3.1
(Percent change, unless otherwise indicated)						
Exports (value)	14.7	32.2	46.6	48.7	27.7	64.5
Non-oil export (value)	36.0	12.8	37.0	3.9	-5.8	11.2
Non-oil export (volume)	41.3	-6.9	7.8	1.1	-12.4	6.5
Imports (value)	6.0	17.8	41.4	42.8	65.8	21.9
Terms of trade	-2.3	8.9	20.8	27.6	24.4	-4.6
Crude oil exports (volume, in millions of barrels)	62.2	72.9	81.2	90.5	80.0	143.3
Sudanese crude oil price (U.S. dollars per barrel) 3/	23.0	27.0	36.4	51.8	49.7	47.4

Sources: Sudanese authorities; and Fund staff estimates and projections.

1/ Includes payments to oil companies as stipulated in production sharing arrangements.

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

3/ Starting from 2006, the reported price is a weighted average of prices for different crude blends.

Table 4. Sudan: Central Government Operations 2002–06

	2002	2003	2004	2005		2006
				Rev. Prog	Year Prel.	Year Prog.
(In billions of Sudanese dinars)						
Total revenues	470.7	741.9	1104.5	1545.9	1472.9	1947.6
Tax revenue	213.4	270.0	420.5	490.0	472.1	571.0
Direct taxes	41.2	52.3	74.7	99.0	92.2	105.0
Indirect taxes	172.2	217.7	345.8	391.0	379.9	466.0
Nontax revenues	257.2	471.9	684.0	1055.9	1000.8	1297.7
Departmental fees	13.0	10.7	14.1	17.8	15.3	25.0
National revenues	244.2	461.2	669.9	1038.1	985.5	1272.7
Non-oil	33.5	38.7	90.6	89.9	84.5	115.0
Oil 1/	210.7	422.6	579.3	948.2	901.0	1157.7
Sales to refineries	99.1	93.1	101.8	288.1	293.3	268.6
Export	83.8	295.9	475.0	660.1	607.7	889.2
o/w OSA	10.1	36.0	84.7	135.0	64.3	114.4
Grants	0.0	0.0	0.0	0.0	0.0	78.9
Total expenditures	346.9	708.4	1019.5	1587.3	1593.9	2018.9
Current expenditures	384.8	563.8	762.5	1374.2	1382.7	1714.4
Chapter one (Wages and salaries) 2/	165.1	191.1	273.8	309.0	301.1	412.3
Chapter two (Other current spending)	186.8	321.3	404.6	639.6	651.0	631.5
Debt service paid	51.1	73.0	81.1	85.9	86.2	120.4
Goods and services	50.5	54.5	71.0	90.1	72.4	107.8
General reserves	50.4	104.0	144.3	155.0	123.3	109.4
Other	34.8	89.8	108.1	308.7	369.1	255.6
Of which: fuel subsidy 3/	0.0	0.0	0.0	200.5	237.5	147.0
Chapter three (Transfers to subnational governments)	32.9	51.4	84.2	425.6	430.7	670.6
Of which: Transfers to the south 4/	...	...	24.0	210.5	190.9	327.5
Capital expenditures	118.6	135.2	277.2	217.7	227.6	304.5
Locally financed	108.9	112.8	227.5	160.8	178.1	186.2
Foreign financed	9.6	22.4	49.7	56.9	49.5	118.3
Discrepancy	-156.5	9.3	-20.2	-4.5	-16.4	0.0
Overall balance	123.8	33.5	85.0	-41.4	-121.1	-71.2
Financing	-123.8	-33.5	-85.0	41.4	121.1	71.2
Foreign financing (net)	9.6	-15.2	5.2	12.1	11.5	50.2
Domestic financing	-133.4	-18.3	-90.2	29.4	109.6	21.1
Central bank	-22.0	-31.9	-85.9	-11.5	46.8	-85.9
Commercial banks	-133.2	12.8	9.0	29.0	29.8	40.0
Nonbanks	19.1	28.7	20.7	49.9	85.1	57.0
Domestic arrears repayment (-)	-8.4	-30.0	-33.9	-48.1	-52.4	0.0
Privatization 5/	11.1	2.1	0.0	10.0	0.3	10.0

Table 4. Sudan: Central Government Operations 2002–06 (Concluded)

	2002	2003	2004	2005		2006
				Rev. Prog.	Year Prel.	Year Prog.
(In percent of GDP)						
Total revenues	11.8	16.1	19.8	22.4	21.8	24.0
Tax revenue	5.4	5.9	7.5	7.1	7.0	7.0
Direct taxes	1.0	1.1	1.3	1.4	1.4	1.3
Indirect taxes	4.3	4.7	6.2	5.7	5.6	5.7
Nontax revenues	6.5	10.2	12.3	15.3	14.8	16.0
Departmental fees	0.3	0.2	0.3	0.3	0.2	0.3
National revenues	6.1	10.0	12.0	15.0	14.6	15.7
Non-oil	0.8	0.8	1.6	1.3	1.3	1.4
Oil 1/	5.3	9.2	10.4	13.7	13.4	14.3
<i>Of which: OSA accumulation</i>	0.3	0.8	1.5	2.0	1.0	1.4
Grants	0.0	0.0	0.0	0.0	0.0	1.0
Total expenditures	8.7	15.4	18.3	23.0	23.6	24.9
Current expenditures	9.7	12.2	13.7	19.9	20.5	21.1
Chapter one (Wages and salaries) 2/	4.1	4.1	4.9	4.5	4.5	5.1
Chapter two (Other current spending)	4.7	7.0	7.3	9.3	9.6	7.8
Debt service paid	1.3	1.6	1.5	1.2	1.3	1.5
Goods and services	1.3	1.2	1.3	1.3	1.1	1.3
General reserves	1.3	2.3	2.6	2.2	1.8	1.3
Other	0.9	1.9	1.9	4.5	5.5	3.2
<i>Of which: fuel subsidy 3/</i>	0.0	0.0	0.0	2.9	3.5	1.8
Chapter three (Transfers to subnational governments)	0.8	1.1	1.5	6.2	6.4	8.3
Transfers to the South 4/	...	...	0.4	3.0	2.8	4.0
Transfers to other states	...	...	1.1	3.1	3.6	4.2
Capital expenditures	3.0	2.9	5.0	3.1	3.4	3.8
Locally financed	2.7	2.4	4.1	2.3	2.6	2.3
Foreign financed	0.2	0.5	0.9	0.8	0.7	1.5
Discrepancy	-3.9	0.2	-0.4	0.0	-0.2	0.0
Overall balance	3.1	0.7	1.5	-0.6	-1.8	-0.9
Financing	-3.1	-0.7	-1.5	0.6	1.8	0.9
Foreign financing (net)	0.2	-0.3	0.1	0.2	0.2	0.6
Domestic financing	-3.4	-0.4	-1.6	0.4	1.6	0.3
Central bank	-0.6	-0.7	-1.5	-0.2	0.7	-1.1
Commercial banks	-3.3	0.3	0.2	0.4	0.4	0.5
Nonbanks	0.5	0.6	0.4	0.7	1.3	0.7
Domestic arrears repayment (-)	-0.2	-0.7	-0.6	-0.7	-0.8	0.0
Privatization 5/	0.3	0.0	0.0	0.1	0.0	0.1
Memorandum Items						
Non-oil revenue 6/	7.0	7.6	10.7	10.4	9.9	10.7
Consolidated expenditures 7/						
Current	5.7	12.4	13.3	18.1	18.2	18.0
Capital	3.0	2.9	5.0	4.9	5.5	6.9
Overall balance (excl. oil savings account)	2.9	-0.1	0.0	-2.6	-2.7	-2.3
Non-oil domestic balance (primary)	-0.7	-5.4	-5.7	-12.3	-13.0	-12.9
Nominal GDP (in billions of Sudanese Dinars)	3,978	4,614	5,573	6,912	6,748	8,107

Sources: Sudanese authorities; and Fund Staff estimates and projections.

1/ From 2005 onwards, oil revenues are reported on an accrual basis and are valued at international prices.

2/ For 2006, the authorities have reclassified about SDD 30 billion (0.4 percent of GDP) of expenditures on wages and salaries to the states from Chapter 3 to Chapter 1.

3/ The gross shortfall in oil revenues from the low consumer prices is accounted for as a subsidy within Chapter Two expenditures. The figure does not include the proceeds from excise taxes on some oil products.

4/ Oil-related transfers as per the peace agreement with the south.

5/ In 2006 the authorities plan to privatize a total of 13 entities including Sudan Telecommunications Company, Sudan Airways, Seaports corporation and the National Building and Construction Company.

6/ Excluding grants. In percent of non-oil GDP. The reduction in the ratio in 2005 reflects a drop in excise rates.

7/ Includes estimated capital spending by subnational governments. Before 2006 a part of the transfers were expenditures carried out by the central government on behalf of the states. Since then, part of Chapter 3 transfers are capital spending by the states.

Table 5. Sudan: Monetary Survey, 2002–06 1/

	2002	2003	2004	2005		2006	
	Dec.	Dec.	Dec.	Dec.	Dec.	June	Dec.
	Actual	Actual		Rev. Prog.	Actual	Prog.	
(In billions of Sudanese dinars, unless otherwise indicated)							
Net foreign assets	-627.0	-570.0	-340.7	-76.5	-58.4	25.8	131.4
Central Bank of Sudan	-741.2	-685.4	-464.8	-246.5	-219.6	-136.7	-29.1
Commercial banks	114.2	115.5	124.1	170.1	161.2	162.5	160.4
Counterpart to valuation changes 2/	796.8	817.0	792.1	721.6	763.9	745.7	729.3
Net foreign assets (excluding valuation adjustment)	169.9	247.1	451.4	645.1	705.5	771.5	860.7
Net domestic assets	392.8	487.0	518.4	632.3	699.9	782.3	935.4
Net domestic credit	329.7	423.8	522.4	687.5	836.9	931.3	1,123.4
Net claims on general government	130.8	111.7	34.7	50.0	48.2	84.5	65.5
Bank of Sudan claims on central government	115.0	83.1	-2.8	-14.3	44.0	-0.8	-41.9
Bank of Sudan claims on the government of the south	0.0	0.0	0.0	0.0	-63.1	0.0	0.0
Commercial banks claims on central government	15.8	28.6	37.6	64.3	67.4	85.4	107.4
Claims on nongovernment sectors	198.9	312.1	487.7	637.5	788.7	846.8	1,057.9
Other items (net)	63.1	63.2	-4.0	-55.2	-137.0	-149.0	-188.0
Broad money	563.3	734.1	969.8	1,277.4	1,403.1	1,553.8	1,796.0
Currency outside banks	193.6	240.2	303.6	347.5	374.0	414.2	502.9
Deposits	369.7	493.9	666.2	929.9	1,029.1	1,139.6	1,293.1
Memorandum items:							
Reserve money (annual percentage change)	22.0	26.6	27.8	29.9	34.9	28.2	25.0
Broad money (annual percentage change)	30.3	30.3	32.1	33.0	44.7	28.0	28.0
Credit to nongovernment sector (annual percentage change)	28.5	56.9	56.2	41.1	61.7	39.2	34.1
Currency to broad money (in percent)	34.4	32.7	31.3	27.2	26.7	26.7	28.0
Foreign currency deposits to total deposits (in percent)	39.6	37.2	37.1	35.3	23.2	23.2	23.2
Broad money multiplier	2.0	2.1	2.1	2.2	2.3	2.2	2.3
Non-oil GDP velocity (average)	7.1	6.6	5.7	4.9	4.8	...	4.2
Commercial banks net foreign assets (in millions of US dollars)	435	443	493	739	685	722	729
Commercial banks credit to the government (cumulative change)	15.5	12.8	9.0	29.0	29.8	18.0	40.0
Vulnerability indicators:							
Capital adequacy ratio 3/	9.0	9.9	10.8	...	12.0	...	...
Ratio of non-performing loans to total loans	12.7	11.4	8.9	...	6.9	...	...
Ratio of loan provisions to bad loans	24.0	22.0	26.0	...	31.9	...	...

Sources: Sudanese authorities; and Fund staff estimates.

1/ For 2005, the monetary survey includes all banks operating in Sudan.

2/ The figures for 2006 are calculated at the program exchange rate.

3/ Including fixed capital.

Table 6. Sudan: Monetary Authorities' Accounts, 2002–06

	2002	2003	2004	2005		2006	
	Dec. Actual	Dec. Actual	Dec.	Dec. Rev. Prog.	Dec. Actual	June Prog	Dec. Prog
(In billions of Sudanese dinars)							
Net foreign assets	-741.2	-685.4	-464.8	-246.5	-219.6	-136.7	-29.1
Foreign assets	119.8	229.7	420.4	573.8	580.4	644.1	734.4
International reserves	63.7	137.1	331.8	...	477.8	675.5	765.8
Other assets	56.1	92.6	88.6	...	102.6	-31.4	-31.4
Foreign liabilities	861.0	915.2	885.1	820.3	800.1	780.8	763.5
Short-term liabilities	43.2	62.2	48.7	...	42.4	56.0	63.0
Medium and long-term liabilities	817.7	853.0	836.4	...	757.7	724.9	700.5
Counterpart to valuation changes 1/	796.1	816.6	788.6	715.1	757.5	739.3	722.9
Net domestic assets	225.3	223.7	129.5	120.1	76.1	97.3	71.1
Net domestic credit	137.1	131.2	42.6	44.9	22.1	53.3	16.1
Net claims on central government	115.0	83.1	-2.8	-14.3	44.0	-0.8	-41.9
Claims	142.2	147.9	148.7	150.6	156.0	162.7	171.0
Deposits	27.3	64.8	151.5	164.9	112.0	163.5	212.9
<i>Of which: oil savings account 2/</i>	...	...	...	135.0	64.4	121.4	178.8
Net claims on government of the south	...	...	...	0.0	-63.1	0.0	0.0
Claims on public enterprises	5.7	17.3	15.5	22.2	19.8	19.8	19.8
Claims on banks	17.1	33.5	30.0	42.0	35.0	36.4	43.2
Money market instruments	-0.8	-2.8	0.0	-5.0	-13.5	-2.0	-5.0
Other items (net)	88.2	92.5	86.9	75.2	54.0	44.0	55.0
Reserve money	280.3	354.8	453.3	588.4	611.7	699.9	764.9
Currency outside banks	193.6	240.2	303.6	347.5	374.0	414.2	502.9
Reserves of commercial banks	75.0	87.2	129.5	197.2	188.9	236.7	247.0
Required reserves	35.2	42.5	57.5	82.8	77.7	98.0	111.2
Excess reserves	39.8	44.7	72.0	114.4	111.2	138.7	135.8
Deposits at Bank of Sudan included in broad money	11.7	27.4	20.2	44.0	48.8	49.0	15.0
Memorandum items:							
Credit to the government (cumulative change)	-22.1	-31.9	-85.9	-11.5	46.8	-44.8	-85.9

Sources: Sudanese authorities; and Fund staff estimates.

1/ The figures for 2006 are calculated at the program exchange rate.

2/ Balance of the new oil savings account of the national unity government (as envisaged in the peace agreement with the south).

Table 7. Sudan: Quantitative Targets Under the 2005 Staff-Monitored Program

	Cumulative Change During 2005						
	2004 1/ Dec.	Jan.-June			Jan.-Dec.		
	Actual	Mid-year Program	Program w/adjustor2/	Actual	End-year Rev. Prog.	Program w/adjustor2/	End-year Est.
(In billions of Sudanese dinars; unless otherwise indicated)							
Central Bank of Sudan net domestic assets	129.5	11.8	-32.1	-34.1	-34.2	36.4	-53.4
Domestic financing of the central government 3/ Contracting or guaranteeing of external nonconcessional debt by the government or the central bank (in millions of U.S. dollars) 4/	-90.2	-6.3	-53.5	15.8	29.4	100.0	109.6
Gross official usable reserves (in millions of U.S. dollars) 5/	310	...	...	803	803	...	935
Payments to the Fund (in millions of U.S. dollars)	1,338	180	358	284	667	360	530
	32.4	15.0	...	16.5	30.0	...	30.3
Memorandum items:							
Broad money	969.8	128.0	...	244.1	316.9	...	433.4
Oil savings account	129.0	32.7	...	76.6	135.0	...	64.4

Sources: Sudanese authorities; and Fund staff estimates.

1/ Outstanding stock at end-2004.

2/ As specified by the technical memorandum of understanding (IMF Country Report No. 05/180, attachment I), the program targets for domestic financing of the budget deficit and for changes in the NDA of the central bank have been reduced, and the international reserves target have been raised by the difference between programmed and actual revenues accumulated in the oil savings account.

3/ Defined as total net borrowing by the government, including net borrowing from the central bank (including Government Musharaka Certificates (GMCs) and changes in deposits of the central government with the central bank but excluding oil savings account), net sales of GMCs outside the central bank, revenues from privatization, and repayments of domestic arrears.

4/ This target applies not only to debt as defined in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274 - (00/85), August 24, 2000), but also to commitments contracted or guaranteed for which value has not been received. Debt 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. The target excludes the financing of the Merowe hydropower project. The end-December target in the revised program has been increased to reflect a higher-than-programmed oil price.

5/ Including foreign banknotes in the vaults of the central bank.

Table 8. Sudan: Structural Benchmarks under the 2005 Staff-Monitored Program

Measures	Status as of end-October 2005
By end-June 2005	
2. Introduce an auction system with competitive selling price for the General Musharaka Certificates (GMC) and General Investment Certificates (GIC) securities in the primary market.	Met
3. Set up and operationalize a single treasury account for all Ministry of Finance's operations.	Met
4. Establish a medium taxpayers' unit.	
5. Develop a program (including timetable) for aligning the SPC and its subsidiaries' accounting systems with commercial standards by end-2006.	Met
	Met
By end-December 2005	
5. Convert the 2006 budget to GFSM 2001 classification.	Delayed, expected May 2006
6. Prepare a 3-year import-tariff reform program and incorporate it in the 2006 budget.	Met
7. Establish a new financing window that allows liquidity constrained banks to sell securities to the central bank at a penalty rate.	Met
8. Prepare a financial sector reform program in light of FSAP recommendations.	Met

Table 9. Sudan: Indicators of Debt Service Capacity, 2002–06

	2002	2003	2004	2005 Prel.	2006 Proj.
(In millions of U.S. dollars; unless otherwise indicated)					
Total debt service paid	137	247	304	279	394
Payments to the Fund	26	28	32	30	45
Charges and interest falling due	17	14	18	17	21
Charges settled	3	1	2	3	2
Reduction in overdue principal obligations	23	26	30	27	43
Overdue obligations to the Fund	1,475	1,576	1,636	1,583	1,559
Overdue obligations to the Fund (in millions of SDRs)	1,085	1,074	1,062	1,054	1,038
Total debt service paid, in percent of:					
Exports of goods and nonfactor services	6.8	9.5	7.9	5.6	4.9
Net current receipts 1/	14.4	16.7	12.9	8.6	8.5
Gross official reserves	55.0	46.9	22.7	14.9	15.3
GDP	0.9	1.4	1.4	1.0	1.1
Payments to the Fund, in percent of:					
Exports of goods and nonfactor services	1.3	1.1	0.8	0.6	0.6
Net current receipts 1/	2.7	1.9	1.4	0.9	1.0
Gross official reserves	10.3	5.3	2.4	1.6	1.8
Quota 2/	11.1	11.1	12.4	12.3	18.5
External debt service paid	18.8	11.2	10.7	10.8	11.4
Available fiscal revenue 3/	1.5	1.0	0.8	0.7	0.9
Overdue obligations to the Fund, in percent of:					
Exports of goods and nonfactor services	74	60	43	32	19
Net current receipts 1/	155	107	70	49	34
Gross official reserves	593	299	122	85	61
GDP	9.8	8.9	7.6	5.7	4.3
External debt	6.2	6.1	6.3	5.7	5.4
Memorandum items:					
Exports of goods and services	1,996	2,613	3,822	4,938	8,050
Net current receipts 1/	952	1,478	2,351	3,262	4,623
Gross official reserves	249	527	1,338	1,868	2,568
In months of next year's imports	1.0	1.5	2.2	2.6	3.1
GDP (in millions of U.S. dollars)	15,109	17,680	21,610	27,699	36,030
Quota (in millions of SDRs) 2/	169.7	169.7	169.7	169.7	169.7
External debt (including arrears)	23,609	25,709	26,001	27,700	28,803
Available fiscal revenue (in millions of U.S. dollars) 3/	1,662	2,646	3,956	4,567	5,032
Exchange rate (U.S. dollar/ SDR, end of period)	1.36	1.47	1.54	1.45	1.43

Source: Fund staff estimates.

1/ Exports of goods and services adjusted for oil related payments for services and transfers to foreign investors.

2/ As percent of Eighth Review Quota.

3/ Domestic fiscal revenue, net of transfers to states.

Table 10. Sudan: External Financing Requirements and Sources, 2002–06

	2002	2003	2004	2005	2006
				Prel.	Proj.
(Cash basis, in millions of U.S. dollars)					
Gross financing requirements	-1,259	-1,228	-1,919	-3,535	-3,663
External current account deficit 1/	-921	-777	-760	-2,511	-2,568
Debt service payments (interest and principal)	-116	-219	-271	-249	-349
Medium and long term debt	-116	-219	-271	-249	-349
Public sector	-116	-219	-271	-249	-349
Multilateral creditors 2/	-29	-60	-66	-57	-77
Paris Club bilateral creditors	0	0	0	0	0
Non-Paris Club bilateral creditors	-88	-159	-204	-192	-272
Other	0	0	0	0	0
Short-term debt	0	0	0	0	0
International reserves accumulation	-197	-204	-855	-745	-700
Payments to the Fund	-24	-28	-32	-30	-45
Financing	1,259	1,228	1,919	3,535	3,663
Official transfers and grants	34	10	28	234	767
Debt financing	45	85	191	309	395
Multilateral	17.2	37	74	133	190
Bilateral	27	48	117	176	205
Foreign direct investment, and errors and omissions	1,256	1,125	1,753	2,670	2,332
IMF purchases and disbursements	0	0	0	0	0
Other flows 3/	-76	8	-54	321	169
Financing gap	0	0	0	0	0
Memorandum items:					
Sensitivity analysis: financing gap assuming:					
Shock 1: Price of oil decline by 10 percent	...	...	...	335	561
Shock 2: Crude production is less by 5 percent	...	...	...	168	285
Shock 3: FDI and net private transfers are 5 percent less than expected	...	...	...	123	193
Combination of all three shocks	...	...	...	626	1,039

Source: Fund staff.

1/ Excludes interest payments and official transfers and includes oil sector profit remittances.

2/ Excluding the IMF.

3/ Includes all other net financial flows.

Table 11. Sudan: Millennium Development Goals, 1990–2003

	1990	1995	2001	2002	2003
1. Eradicate extreme poverty and hunger					
Population below \$1 a day (percent)	...	...	...	...	...
Poverty gap ratio at \$1 a day (percent)	...	...	...	...	...
Percentage share of income or consumption held by poorest 20 perce	...	...	...	...	...
Prevalence of child malnutrition (percent of children under 5)	...	...	...	...	...
Population below minimum level of dietary energy consumption	...	...	...	27.0	...
2. Achieve universal primary education					
Net primary enrollment ratio (percent of relevant age group)	43.3	...	...	...	...
Percentage of cohort reaching grade 5 (percent)	93.8	...	84.3	...	...
Youth literacy rate (percent ages 15-24)	...	...	...	...	...
3. Promote gender equality					
Ratio of girls to boys in primary and secondary education (percent)	77.4	...	...	85.8	...
Ratio of young literate females to males (percent ages 15-24)	...	...	...	...	...
Share of women employed in the nonagricultural sector (percent)	22.2	20.4	19.3	19.1	18.9
Proportion of seats held by women in national parliament (percent)	...	...	...	10.0	10.0
4. Reduce child mortality					
Under 5 mortality rate (per 1,000)	120.0	106.0	...	...	93.0
Infant mortality rate (per 1,000 live births)	74.0	69.0	...	...	63.0
Immunization, measles (percent of children under 12 months)	57.0	51.0	67.0	49.0	57.0
5. Improve maternal health					
Maternal mortality ratio (modeled estimate, per 100,000 live births)	...	...	...	...	...
Births attended by skilled health staff (percent of total)	69.4	...	...	...	...
6. Combat HIV/AIDS, malaria and other diseases					
Prevalence of HIV, female (% ages 15-49)	...	...	3.1	...	...
Contraceptive prevalence rate (% of women ages 15-49)	8.7	...	...	...	...
Number of children orphaned by HIV/AIDS	...	...	...	...	...
Tuberculosis prevalence rate (per 100,000 people)	179.3	193.9	212.9	216.2	219.6
Tuberculosis cases detected under DOTS	...	...	31.4	32.9	33.7
7. Ensure environmental sustainability					
Forest area (percent of total land area)	30.0	...	...	...	...
Nationally protected areas (percent of total land area)	...	...	...	...	5.2
GDP per unit of energy use (PPP \$ per kg oil equivalent)	2.2	3.0	3.9	3.8	...
CO2 emissions (metric tons per capita)	0.1	0.1	...	...	...
Access to an improved water source (percent of population)	64.0	...	...	...	69.0
Access to improved sanitation (percent of population)	33.0	...	...	34.0	...
Access to secure tenure (percent of population)	...	...	...	...	...
8. Develop a Global Partnership for Development					
Youth unemployment rate (percent of total labor force ages 15-24)	...	...	...	...	...
Fixed line and mobile telephones (per 1,000 people)	2.5	2.8	17.5	26.5	46.6
Personal computers (per 1,000 people)	...	0.4	3.6	6.1	...
General indicators					
Adult literacy rate (percent of people ages 15 and over)	...	...	...	...	...
Total fertility rate (births per woman)	5.4	5.1	5.1	4.4	4.4
Life expectancy at birth (years)	52.2	...	...	58.4	58.6
Aid (percent of GNI)	6.6	3.9	1.5	2.5	3.8

Source: World Bank, World Development Indicators.

RELATIONS WITH THE FUND

(As of February 28, 2006)

I. Membership Status: Joined 09/05/57; Article VIII.

II. General Resources Account:	<u>SDR Million</u>	<u>% Quota</u>
Quota	169.70	100.00
Fund holdings of currency	469.59	276.72
Reserve position in Fund	0.01	0.01

III. SDR Department:	<u>SDR Million</u>	<u>% Allocation</u>
Net cumulative allocation	52.19	100.00
Holdings	0.00	0.00

IV. Outstanding Purchases and Loans:	<u>SDR Million</u>	<u>% Quota</u>
Stand-by Arrangements	179.62	105.85
Extended Arrangements	100.70	59.34
Contingency and Compensatory Financing Facility	19.55	11.52
Trust fund	59.23	34.90

V. Financial Arrangements:

	Approval	Amount	Amount Approved	Drawn
Type	Date	Expiration Date	(SDR million)	(SDR million)
Stand-by	06/25/1984	06/24/1985	90.00	20.00
Stand-by	02/23/1983	03/09/1984	170.00	170.00
Stand-by	02/22/1982	02/21/1983	198.00	70.00

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

	Overdue ¹⁹ 2/28/06	<u>Forthcoming</u>				
		2006	2007	2008	2009	2010
Principal	359.10					
Charges/Interest	<u>694.90</u>	<u>12.06</u>	<u>16.04</u>	<u>16.06</u>	<u>16.03</u>	<u>16.04</u>
Total	1,054.00	12.06	16.04	16.06	16.03	16.04

¹⁹ The projection of charges and interest assumes that overdue principal at the report date (if any) will remain outstanding, but that forthcoming obligations will be settled on time.

VII. Exchange Rate Arrangements

The legal tender is the Sudanese dinar, which replaced the Sudanese pound in proportion SDD 1=LSd 10 in 1999. Since October 1998, the exchange rate system has been unified—market participants trade freely within a unified regulatory framework. In 2001, the foreign exchange market came under pressure and the Central Bank of Sudan (CBOS) introduced a formal band of ± 1.5 percent (later broadened to 2 percent) around the official rate and began auctioning its foreign exchange within the band. In May 2003, the CBOS adopted a managed-floating exchange rate regime. The formal exchange rate band was abandoned and the auction system was replaced with direct transactions in the interbank market. The CBOS established an internal limit of ± 2 percent in intraday trading in the average daily market rate. In 2004, the CBOS changed the permissible intraday exchange rate fluctuation from ± 2 percentage points to ± 3 percentage points. Sudan maintains one inoperative bilateral payment agreement with Egypt and an inoperative payment clearing account with the former Soviet Union. Sudan maintains an exchange system that is free of restrictions on the making payments and transfers for current international transactions.²⁰

VIII. Article IV Consultation

Sudan is on a 12-month consultation cycle. The last Article IV consultation discussion was completed by the Executive Board on April 29, 2005 (IMF Country Report No.05/180).

IX. FSAP Participation

The FSAP work took place during October 9-14, 2004 and was completed during December 1–14, 2004. The Financial System Stability Assessment report was discussed by the Executive Board on April 29, 2005.

X. Resident Representative

The Fund's resident representative office in Khartoum was reopened in October 2005, as a shared post with Djibouti.

XI. Technical Assistance

In January 1995, the Executive Board decided to resume Fund technical assistance to Sudan. The following table contains a summary of the technical assistance provided since 2002.

²⁰ In November 2005, the authorities removed two remaining exchange restrictions under Article VIII, Sections 2, 3 and 4 of the Fund's Articles of Agreement. At that time, they lifted the prohibition that applies to importers in arrears with valid import licenses from executing payments and transfers for import transactions and eliminated the multiple currency practice arising from the use of a historic buying rate for the resale of export proceeds.

Sudan: Technical Assistance from the Fund, 2002–2006

Subject	Type of Mission	Timing	Counterpart
Fiscal Affairs Department			
Expenditure control and management	Short-term	Periodic visits January–September 2002	Ministry of Finance (MOF)
Reform of direct taxation and revenue administration	Short-term	November 2002 and December 2003	MOF
Reform of direct taxes and investment incentives	Short-term	March 2003	MOF
Medium-term budgetary framework	Short-term	April 2003	MOF
Tax and customs administration	Short-term	September 2003	MOF
Fiscal cash management and budget classification	Short-term	February 2004	MOF
Fiscal cash management and budget classification (METAC)	Short-term	May and September 2004 June and October 2005	MOF
Revenue administration assessment (METAC)	Short-term	February 2005	MOF
Revenue administration (METAC)	Short-term	October 2005	MOF
Monetary and Financial Department			
Monetary management and banking supervision	Short-term	Periodic visits, January-August 2002	Central Bank of Sudan (CBOS)
Banking supervision	Resident Advisor	May 2001–May 2003	CBOS
Islamic compliant monetary instruments	Short-term	October 2002	CBOS
Monetary policy operations and introduction of a commodities futures/forward market in the agriculture sector	Short-term	December 2003	CBOS
Monetary policy operations	Short-term	September 2004	CBOS
Introduction of new national currency	Short-term	February 2005	CBOS
Introduction of new national currency: Assessment of circulating currencies in Sudan	Short-term	March-April 2005	CBOS
Banking supervision (METAC)	Short-term	August 2005	CBOS
Reorganization of the Bank of Sudan	Short-term	August-September 2005	CBOS
Assessment of technical assistance needs on microfinance supervision and regulation	Short-term	December 2005	CBOS
Introduction of new national currency	Short-term	January-February 2006	CBOS
Statistics Department			
Monetary statistics	Short-term	Periodic visits, January-November 2003	CBOS
National accounts and CPI statistics	Short-term	Periodic visits, March 2002-February 2003	Central Bureau of Statistics (CBS)
Balance of payments statistics	Short-term	July 2003	CBOS
General data dissemination system (GDDS)	Short-term	July 2003	CBS, MFE and CBOS
Assessing technical assistance needs in economic statistics (with METAC)	Short-term	May–June 2005	CBS, MOF and CBOS
Government Financial Statistics	Short-term	October 2005	MOF
Monetary and Financial Statistics	Short-term	November-December 2005	CBOS

SUDAN: RELATIONS WITH THE WORLD BANK²¹

(As of March 17, 2006)

The World Bank has no active lending portfolio in Sudan because of Sudan's default on its financial obligations to the Bank, which led to the suspension of disbursements in April 1993. After discussions between the Bank and the Sudanese authorities on the need for Sudan to take steps toward normalizing its relations and establishing a track record with the Bank, the authorities started making "good faith" payments of US\$1 million per month to the Bank since July 1999 and US\$500,000 per month since October 2002. The amount of payments has not been sufficient to prevent a continued accumulation of arrears, which stood at about US\$372 million as of March 16, 2006 (from US\$145 million at the end of 1999). Sudan's outstanding Bank debt, including arrears, is approximately US\$1.3 billion.

The Bank was mostly absent from Sudan between 1992 and 2002. In the 1970s and 1980s, the Bank was a major player in the reconstruction of Sudan, following the Addis Ababa peace agreement of 1972. As the prospects for peace with the South rose in 2003, the Bank formulated a strategy for reengaging with Sudan in the event of peace. This strategy, described in the Sudan Country Reengagement Note (CRN), was discussed by the Executive Board of Directors on July 10, 2003. Main areas of emphasis in the CRN are knowledge generation and sharing, capacity building to support policy reform, demonstration projects to improve delivery of social services, and resolution of the debt overhang. In addition to capacity building, the Bank, together with the Fund, provided technical resource persons for the discussions around wealth sharing in the peace talks. The Bank is also providing technical support to the Darfur peace talks in Abuja, Nigeria.

Between January 2004 and March 2005, the Bank co-led (with the UN) a Joint Assessment Mission (JAM), covering eight thematic sectors.²² IMF staff participated in a number of workshops and contributed to the economic policy cluster. The JAM synthesis report: "Framework for Transition, Reconstruction and Poverty Eradication," was completed in March 2005. The Report outlines the reconstruction and development needs for Sudan over the six year Interim Period as well as a Monitoring Framework that reflects policy reforms and commitments made by the government which are needed to implement the Comprehensive Peace Agreement (CPA). The Report, presented at an April 2005 Donors' Conference in Oslo, raised US\$2.0 billion in pledges for 2005–2007.

To report on progress on policy commitments and to renew financial pledges, it was agreed that a twice-yearly Sudan Consortium meeting would be held. The first meeting of the Consortium took place in Paris on March 9 and 10, 2006. During the Consortium, the

²¹Prepared by World Bank staff. **For additional information, contact Ms. Jill Armstrong, Country Program Coordinator for Sudan, Tel. (202) 473-8471.**

²² The full report is posted at: <http://www.unsudanig.org/JAM>.

government reported on progress and an assessment made by the Bank, IMF and UN laid out the joint views of staff with respect to the credibility and implementation of the policies and programs, key constraints, and proposed next steps. Particular attention was paid to the need for improved public expenditure and revenue management at all levels of government as well as good governance. The broad conclusion was that progress is being made in implementation of the CPA, although there have been delays (i.e. need for effective functioning of the National Petroleum Commission and other institutions). The centrality of poverty eradication and the MDGs was reaffirmed; however, the government must follow through with the implementation of commitments on pro-poor development. Donors also reconfirmed the levels of financial pledges made at the 2005 Oslo Donors' Meeting.

The Comprehensive Peace Agreement agreed between the government of Sudan and the Sudan People's Liberation Movement (SPLM) specified that two Multi-Donor Trust Funds (MDTFs) be established to facilitate the coordination of external donor financing of Sudan's reconstruction and development needs as laid out in the JAM. One fund would be for the new National Government (NG) for war-affected areas in the north and the transition zones, and one for the government of Southern Sudan (GoSS). The MDTFs would remain operational through the six years of the Interim Period. MDTF-financed activities would be within the context of a unified budget and a coherent public expenditure process. Approximately US\$500 million was pledged in Oslo toward two Trust Funds, nearly all of which has been formally committed over 2005-2007. The World Bank is the Administrator for both MDTFs. The MDTFs are now effective and the first projects have been approved.

As part of the JAM, a workshop with the government and the SPLM initiated work on a joint strategy for poverty eradication (PRSP). IMF staff also participated. During this workshop, the parties reached an agreement on a shared vision for poverty eradication, with an articulation of strategic objectives and associated operational implications. A joint concept note was developed that provides the foundation for a national Poverty Eradication Strategy. Based on this work, the interim PRSP is expected to be finalized in 2006.

To support capacity building and policy reform, a US\$4.5 million Low-Income Countries under Stress (LICUS) trust-fund grant for Sudan was approved in December 2004. The grant focuses on capacity building and institutional development of fiduciary and aid-management systems both in the North and in the South. The trust fund complements two ongoing Post Conflict Fund grants from the World Bank totaling US\$3.0 million.

The World Bank is also preparing a Public Expenditure Review (PER), with selected broad activities, which are distinct for the NG and the GoSS. The proposed approach is pragmatic in that a series of distinct activities are being designed to build joint understanding and ownership and to begin to address capacity-building needs through end-2007. IMF staff will participate in this work in the areas of their competence. Lastly, World Bank staff is working at a technical level with the IMF and other multilateral creditors to explore options for clearance of arrears and debt relief.

SUDAN: STATISTICAL ISSUES

Available economic data are generally adequate for surveillance and program monitoring. However, there are many areas where further improvements are needed, particularly in compiling national accounts, state budgetary data, and external trade and financial statistics. This appendix discusses outstanding statistical issues by sector.

As a participant in the Department for International Development (DFID) project for Anglophone African countries, Sudan has been receiving technical assistance in various statistical issues. DFID financed three Statistics Department (STA) missions in June–July 2003 (monetary and financial statistics, balance of payments statistics, and the General Data Dissemination System (GDDS) metadata completion), contributing to Sudan’s participation in the GDDS starting in August 2003.

In early 2004, Sudan also received assistance for the initial stages of preparation of a strategic plan for the Central Bureau of Statistics (CBS). In May 2005, an STA/METAC mission assessed the technical assistance needs in macroeconomic statistics and identified emerging statistical priorities in the statistics-producing agencies. In December 2005, a follow-up mission on monetary and financial statistics visited Khartoum to assist the authorities in further implementing the action plan developed by the mission in 2003.

I. REAL SECTOR

In recent years, practices in the production of the monthly Consumer Price Index (CPI) have been commendable. Monthly CPI data for the Khartoum area are provided shortly after the end of each month, while the CPI for other states is provided with a three-month lag.

The compilation of the national accounts is subject to delay. The national accounts statistics suffer from a lack of basic information for many sectors, including oil, livestock, horticulture, and most services. On the expenditure side, data are lacking on final consumption by households, investment, and changes in stocks. There are no national accounts or industrial production data at sub annual frequencies. Furthermore, the annual data are being reported with a lag of over three years. There is an urgent need to increase funding to the CBS and rebuild its capacity. Priorities include introducing the *1993 System of National Accounts*, conducting a census of agricultural production, carrying out a household survey, producing poverty statistics, and improving coordination between the CBS, the Ministry of Finance and National Economy (MOFNE), the Ministry of Energy and Mining, and the Ministry of Agriculture and Livestock. A peripatetic real sector expert provided technical assistance on national accounts through end-2003.

II. FISCAL SECTOR

Government Finance Statistics are broadly adequate for program monitoring, with the main revenue, expenditure, and financing items reported on a monthly basis with a lag of about one month. Financing items are consistent with the monetary accounts. The reported statistics are for the central government only, and do not include the states and publicly owned corporations. Data are submitted using an outdated economic classification and, while the allocation of resources by MOFNE to the various ministries is reported, their actual expenditures are not. There is an urgent need to improve accounting and reporting procedures, introduce GFS classifications according to guidelines provided in the *Government Finance Statistics Manual (GFSM) 2001*, and implement technical assistance recommendations on GFS. Monthly and quarterly fiscal data are not reported for the *Government Finance Statistics Yearbook* or for the *International Financial Statistics (IFS)*. The October 2005 mission assisted the authorities in developing a budget classification and budget execution reports in line with the GFSM 2001 methodology.

III. MONETARY SECTOR

Sudan has received significant technical assistance to improve the collection, compilation, and dissemination of monetary and financial statistics. The most recent STA mission took place in December 2005, and assisted in implementing the ongoing action plan. Progress has been made in several areas including finalizing the new report form and its accompanying guidelines, which were scheduled for pilot testing during the first quarter of 2006. The weekly flash report on the activities of the Central Bank of Sudan (CBOS) is consistent with relevant components in the depository corporations' survey as recommended in the *Monetary and Financial Statistics Manual*.

In general, the monetary statistics compiled by the CBOS are acceptable for monitoring purposes. However, the central bank should complete the harmonization of its accounting codes and network connections as this would improve data collection and compilation. In addition, the central bank should work with the Ministry of Finance to review and reconcile government accounts held with the banking system to ensure their appropriate classification in the monetary survey. There is also a need to develop a framework for future collection and incorporation of South Sudan's banking activities into the monetary statistics. Another follow-up mission on monetary and financial statistics to Sudan will be considered after the authorities have completed the priority actions recommended by the December 2005 mission.

IV. EXTERNAL SECTOR

Daily exchange rate data are reported to the Fund with minimal lags, but there are several areas for improvement in the external accounts, particularly with regard to foreign direct investment, trade, and oil statistics. The authorities need to provide clarification on items that qualify as international reserves in general, and those earmarked reserves in particular, and

should begin compiling the data template on international reserves and foreign currency liquidity.

Regarding import statistics, there are significant discrepancies between the reports from customs and from the central bank. The July 2003 STA mission identified some possible causes and, in collaboration with the authorities, attempted to reconcile the data. The mission reported some progress on implementing previous STA recommendations. However, the lack of survey data continues to affect the compilation of important balance of payments items such as foreign direct investment.

Medium-term oil production projections and data on amortization of private sector debt need substantial improvement. The authorities have made some progress in improving oil projections, but need to provide more detailed information on the phasing-in and expected production levels of new blocks and on amortization of debt in the oil sector.

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 the Central Statistics Office.	Broadly acceptable: Real and nominal GDP by sector available with a 2-year lag.	1968 System of National Accounts (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 most GDP components.	Rebuild the Central Bureau of Statistics' (CBS) institutional capacity; introduce the 1993 SNA; conduct census of agricultural production. Implement the project prepared by the STA's peripatetic real sector expert.
	Last and current year estimates reported to missions by the ministry of finance and national economy (MOFNE).	Acceptable.	Estimates are based on incomplete data, in particular for oil value added, livestock, and fruit and vegetable production.	Improve coordination between MOFNE, CBS, and the ministry of agriculture.
Prices	Monthly CPI reported on time, with a minimal lag.	Acceptable; only CPI for Khartoum area available promptly; weekly CPI published in the flash report.	CPI for Sudan as a whole is not available.	Conduct new household income and expenditure survey; reduce timing discrepancies and other reporting inefficiencies by individual states.
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.	Only partial data on state budgets available; incomplete functional classification; MOFNE allocations to ministries are reported, but not their actual expenditure; slow progress on the introduction of the government finance statistics (GFS) classification.	Introduce the GFS classification; improve accounting and reporting procedures at MOFNE. Implement in full GFS (1997) technical assistance (TA) mission recommendations.
Monetary accounts	Monthly reporting of balance sheets. Generally on time; 1.5-month lag.	Acceptable following recent STA missions to improve transparency and reliability of the monetary statistics.	Large and variable other items (net); frequent misclassification errors by commercial banks, in particular for consortium financing, which prevents meaningful analysis of the composition of net domestic assets (NDA).	Establish a working group to review the Central Bank of Sudan's (CBOS) foreign assets; review and revise the guidelines related to consortium financing and ensure compliance. Implement the 2001 TA mission on monetary statistics recommendations, including improvement of commercial banks' other items (net).

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; estimates of usable reserves of CBOS added in January 2003.	Some divergence between reserve money in balance sheets and end-of-month flash reports.	Include data on returns on investment deposits. Aim at full reporting of the CBOS balance sheet.
External sector: foreign exchange reserves	Monthly reporting of CBOS active balances. Generally on time; 0.5-month lag.	Acceptable, but needs improvement; frequency of monitoring should increase to weekly; quality of data needs to be strengthened.	Gross usable reserves are part of CBOS 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 the case of a balance of payment need are not clear.	Clarify the items that qualify as international reserves in general and those included in earmarked reserves in particular.
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 the residency criterion; enhance institutional capacity of the CBOS BOP compilation unit. Implement in full the recommendations of the 1999 and 2003 TA in BOP statistics.
	Monthly trade data; upon request provided with a 2–3 month lag.	Acceptable, but needs improvement.	Discrepancies between CBOS data and customs data.	
External debt	Monthly payments to creditors. On time; 1.5-month lag.	Good; CBOS cash flow table is not available.	CBOS cash flow table does not reflect exactly actual payments made by the MOFNE.	Eliminate timing and recording discrepancies between the CBOS and the MOFNE.
	Other debt data; 10-month lag.	Good; coverage is comprehensive, although weaknesses in some areas persist.	CBOS records are not reconciled with those of some creditors; data on Official Development Assistance not available; charges 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; Debt Management Unit to send monthly statements on external debt to the CBOS's Statistics Department.

SUDAN: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE
AS OF MARCH 17, 2006

	Date of latest observation	Date received	Frequency of data ⁶	Frequency of reporting ⁶	Frequency of publication ⁶
Exchange Rates	3/11/06	3/12/06	D	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities ¹	1/31/06	3/18/06	M	M	M
Reserve/Base Money	1/31/06	3/18/06	M	W	M/W
Broad Money	1/31/06	3/18/06	W	W	M/W
Central Bank Balance Sheet	1/31/06	3/18/06	M	M	M
Consolidated Balance Sheet of the Banking System	1/31/06	3/18/06	M	M	M
Interest Rates ²	Feb. 2006	3/18/06	W	M	M/W
Consumer Price Index	Feb. 2006	3/18/06	M/W	M	M
Revenue, Expenditure, Balance and Composition of Financing ³ – General Government ⁴	Jan. 2006	3/18/06	M	M	M
Stocks of Central Government and Central Government-Guaranteed Debt ⁵	Dec. 2005	Feb. 2006	A	A	A
External Current Account Balance	2005: Q4	Feb. 2006	Q	Q	Q
Exports and Imports of Goods and Services	2005: Q4	Feb. 2006	M	M	M
GDP/GNP	2005	Feb. 2006	A	A	A
Gross External Debt	2005:Q4	Feb. 2006	A	A	A

¹Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.

²Both market-based and officially determined, including discount rates, money market rates, and rates on treasury bills, notes and bonds.

³Foreign, domestic bank, and domestic nonbank financing.

⁴The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

⁵Including currency and maturity composition.

⁶Daily (D); Weekly (W); Monthly (M); Monthly/Weekly (M/W); Bi-monthly (B); Quarterly (Q); Annually (A); Irregular (I); Not Available (NA)

March 9, 2006

Mr. Rodrigo de Rato
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Mr. de Rato,

Slightly more than a year ago a historical peace agreement was signed that ended more than twenty years of civil war between the north and the South of Sudan. Implementation of the Comprehensive Peace Agreement is now underway and we have formed a new government of national unity. This government has now turned its efforts to peacefully resolving the Darfur crisis. To this effect, we have been an active and good faith party in the peace talks currently held in Abuja.

Meanwhile we have sought to implement economic policies that aim at maintaining economic stability, fostering growth, and reducing poverty. We believe these will be important factors in promoting peace and reconciliation throughout the country. We appreciate in that respect the close and long-standing policy dialog with the Fund. Discussions with Fund staff on the 2006 Article IV consultation, and on a new Staff Monitored Program for 2006 were conducted in Khartoum in February 2006.

The attached Memorandum of Economic and Financial Policies (MEFP) sets forth our policy intentions under the 2006 SMP. We are committed to maintain macroeconomic stability and advance the reform agenda. The government believes that these policies are adequate to achieve the objectives of the program and will consult with the Fund on any revision of the policies contained in the MEFP. Notwithstanding the enormous financing needs for national reconstruction and peace that we face, and to strengthen our cooperation, we propose to increase our payments to the Fund from \$30 million in 2005 to \$45 million in 2006.

We are committed to a process of economic integration both within Sudan and with the international community, but our success depend also on the support we get from multilateral institutions and development partners. In this regard, we look forward to the Fund's Executive Board's discussion of the SMP and to the resolution of Sudan's debt and arrears problems in the near future. In the meantime, we will intensify our efforts to obtain financing assurances from creditors for arrears clearance and debt relief under the Heavily Indebted Poor Countries and the Multilateral Debt Relief Initiatives.

Sincerely yours,

/s/
Al- Zubeir Ahmed AL-Hassan
Minister of Finance and National Economy
Ministry of Finance and National Economy

/s/
Dr. Sabir Mohamed Hassan
Governor
Central Bank of Sudan

GOVERNMENT OF SUDAN
Memorandum of Economic and Financial Policies
March 9, 2006

1. This memorandum sets out the economic policies and objectives of the government of National Unity for 2006. These policies will be pursued in the context of an IMF staff-monitored program (SMP) for 2006.

I. RECENT DEVELOPMENTS

2. Despite the tremendous challenges we faced in the first year of implementation of the Comprehensive Peace Agreement (CPA), we have tried to maintain the thrust of our economic policies, achieved high economic growth, and contained inflationary pressures. In 2005, GDP growth is estimated at 8 percent while average inflation was contained at 8.5 percent. High oil prices supported the balance of payments and allowed for a further accumulation of international reserves. Economic stability, robust growth, and a stronger balance of payments led to an 8 percent appreciation of the Sudanese dinar against the U.S. dollar.

3. Fiscal performance was weaker than programmed, owing primarily to the expanding fuel subsidy.¹ Although higher than in 2004, oil revenues were also lower than programmed because of a delay in commencing oil production in Blocks 3 and 7. In addition, non-oil revenues were below projection because of an increase in the volume of imports exempted from VAT (capital goods and NGO-related imports). The lower-than-programmed revenues and higher expenditures led to a withdrawal of deposits from the oil savings account and higher-than-programmed non-bank financing (mostly government securities). Following the stipulations of the CPA, we initiated transfers to the government of South Sudan.

4. Broad money during the year grew by 45 percent, while reserve money growth increased by 35 percent. Both variables exceeded the programmed amounts because of high foreign exchange inflows and an expansionary fiscal stance. Private sector credit also increased rapidly during the year (62 percent).

5. We undertook a number of structural reforms in the fiscal arena. To enhance non-oil revenues, a medium taxpayer unit was set up early in the year. A three-year tariff reform program was prepared and the first phase of the reform was initiated in the 2006 budget. In customs administration, we adopted the ASYCUDA++ and plan to implement risk based verification system later this year. We continued our efforts to strengthen cash management

¹ The prices of most domestically consumed fuels were set when the 2005 budget was formulated and remained unchanged since then despite rising international prices. These prices are traditionally set by decree and are not automatically adjusted in response to changing market conditions. The SPC discounts the difference between domestic and world prices when it transfers oil revenue to the treasury. This way of handling the oil subsidy will be addressed in future fiscal execution reports and budgets by presenting the subsidy as an expenditure item.

by the preparation of a cash plan on a regular basis and improving coordination between the ministry of finance and the central bank through regular high-level meetings. Notwithstanding our efforts, we acknowledge that further improvements in cash management are warranted.

6. Banking system soundness indicators improved in 2005. While credit expanded rapidly during the year, the ratio of nonperforming loans to total loans decreased from 8.9 percent in December 2004 to 6.9 percent at end-2005. The asset quality of banks also improved. As of December 2005, a total of 18 banks (out of 24 banks) complied with capital adequacy requirements. As for the concentration of credit, almost 40 percent of the increase in credit to the private sector was granted by a single bank. We have put this bank under close supervision to monitor its lending activities.

7. Regarding monetary operations, we began auctioning Government Musharaka Certificates (GMCs) and Government Investment Certificates (GIC) through competitive tenders without predetermined prices, phased out the existed financing window for banks, and implemented the new financing window by using collateral-based certificates. We also launched the Central Bank Ijara Certificates (CIC) in the fourth quarter of 2005 to help manage short-term liquidity. During 2005, we privatized the Khartoum Bank and granted four new licenses for commercial banks: Al-Salam Bank, the Egyptian Sudanese Bank, Capital Bank, and the Emirate Sudanese Bank. The restructuring of the central bank to function within a new federal banking system has already begun with the Central Bank of Sudan (CBOS) changing its legal structure and the approval of new laws for the central bank and for commercial banks. Lastly, the CBOS has established its branch in Juba as envisaged in the CPA.

8. Despite a number of difficulties related to the first year of implementation of the peace agreement with the South, we made every effort to meet the targets under the Staff-Monitored Program and met three of the five quantitative targets for end-December and all but one of the structural benchmarks. The quantitative target on the financing of the fiscal deficit was missed by a small margin, while the target on nonconcessional borrowing was missed as new loans for US\$122 million were contacted in the second half of the year. These loans were needed to finance critical water and social projects and were contracted as we had limited access to concessional financing and grants. Regarding the conversion of the 2006 budget into GFSM 2001 format (end-December structural benchmark), we have not been able to proceed as fast as planned because of complexities in the preparation of the 2006 budget, which in turn are related to the implementation of the new revenue sharing arrangements under the CPA. However, given the importance of this reform, we will implement this measure by May 2006.

II. MEDIUM-TERM OUTLOOK AND CHALLENGES

9. The CPA provides a good framework for building a prosperous and peaceful Sudan. Despite initial unavoidable delays, we are fully committed to implement the agreement, tackling regional inequalities, and reducing poverty. In this regard, we launched a strategy

to meet the Millennium Development Goals and intend to finalize our interim Poverty Eradication Strategy by the end of this year. We will also continue to reorient public spending toward disadvantaged regions and social and infrastructure projects as well as on capacity building and the revamping of public financial management systems at all levels of government. We are committed to clear arrears and achieve debt sustainability, but we will need comprehensive and deep debt relief beyond traditional mechanisms.

10. Meeting Sudan's medium term challenges will require economic stability, sustained growth, the spread of peace throughout the country, and regularization of relations with donors and creditors. We are committed to prudent macroeconomic policies and a new wave of structural reforms to strengthen the business environment, foster agricultural development, and improve transparency in the oil sector as well as in the use of public resources. This will require improvements in policy coordination between (and within) national and subnational governments as well as capacity building. Notwithstanding higher oil revenues, fiscal policy will mobilize non-oil revenues to lower the dependence on oil revenues and preserve a prudent fiscal policy. The medium-term outlook envisages economic growth of 8–10 percent per year, a continued decline in inflation to 5 percent or less by 2008, and reductions in poverty levels.

III. OUTLOOK AND POLICIES FOR 2006

11. The 2006 program of the national government assumes economic growth of 13 percent, bolstered by a large increase in oil production and continued high growth in the non-oil sector. The average inflation objective is 7.5 percent, compared to 8.5 percent in 2005.

12. **Fiscal policy.** The fiscal deficit (including grants) will be contained at no more than 0.9 percent of GDP as both revenue and expenditure increase rapidly. On the revenue side, oil revenues will increase because of high international oil prices and higher output. For budget purposes, the benchmark price of oil has been set at US\$45 per barrel for the Nile blend crude and US\$40 for the new DAR blend crude. Non-oil revenues will benefit from improvements in administration, including improvement in collections in the South and other states, and from a rationalization of tax exemptions (see below). On the expenditure side, the recently approved budget figures have been revised because they were based on unfeasible assumptions about the size of the oil subsidy. Compared to the budget figures, we will contain the intended large increase in civil servants' salaries, expenditures on goods and services, transfers to the northern states, and domestically financed capital expenditures, to ensure that the fiscal framework is compatible with our goal of economic stability. This will be done in a manner that protects proposed spending on programs that directly benefit the poor—namely pro-poor development spending. Further, any shortfall in non-oil revenues will be covered by restraint in lower priority expenditures from Chapter I and Chapter II. We hope that increased development assistance from the international community in 2006 will also help co-finance pro-poor programs. We will inform parliament of these changes vis-à-vis the budget as no supplementary budget will be required.

13. **Fuel subsidies.** We intend to review the policy on domestic fuel prices this year to reduce the sizeable subsidy. We realize that these subsidies do not benefit the poor, distort the allocation of economic resources, contribute to environmental problems, and compromise other valuable expenditures. Still, we will ensure the public is well informed about this policy action. Later this year, we will also finalize a strategy to eliminate these subsidies and adopt an automatic mechanism that passes through changes in world prices of crude to product prices.

14. **Monetary policy.** The program will target a broad money growth rate of 28 percent in 2006, consistent with GDP growth and inflation objectives, and an increase in money demand reflecting the reintegration of the South. The monetary target and the projected build-up in foreign reserves will allow for an appropriate growth rate of credit to the nongovernmental sector. The conduct of monetary policy will be challenging given a number of uncertainties, including the fiscal behavior of national and sub-national governments, introduction of the new currency, the size of the private capital movements, and large oil export receipts. Accordingly, we expect to reassess the monetary targets mid-year to ensure that it remains in line with the program's inflation objective.

15. **Monetary operations.** We will rely heavily on open market operations for supporting banks' liquidity needs and government and central bank securities will continue to be issued in competitive auctions. Direct lending to banks will be limited and collateralized by short-term securities, while lending to public enterprises (including for agriculture) will remain at its end-2005 level.

16. **Exchange rate flexibility.** As exchange rate appreciation pressures are likely to continue, we will ensure exchange rate flexibility to safeguard our inflation objective. The envisaged fiscal expansion for 2006 will exert pressure on monetary aggregates and on inflation, which will need to be appropriately sterilized through open market operations and/or foreign exchange operations.

17. **Competitiveness.** High external inflows and an expansionary fiscal stance have recently led to an appreciation of the real exchange rate, which in turn appears to have been partly responsible for a decline in non-oil exports in 2005. As these trends are expected to persist, we will intensify our efforts to improve the business environment for the private sector through the removal of structural bottlenecks (especially on transportation) and other institutional reforms as well as efforts to foster rural development. In this regard, we will be conducting an investment climate assessment with the assistance of the World Bank. The assessment will identify key areas of improvement as well as indicators to be tracked over time.

18. **Tax policy and administration.** To protect our tax base, the Ministry of Investment will not refer to the Council of Ministers any proposal to renew expired business profit tax exemptions granted under the Investment Encouragement Act. By October 2006, we will finalize a program to revamp the system of investment incentives in consultation with Fund staff and in line with best international practice. The program will also address the need to

adopt a uniform system of profit tax rates to ensure a level playing field for investors across sectors. Lastly, we will examine the scope for expanding the VAT base by bringing exempted items into the tax net. In the area of tax administration, key measures include the introduction of self-assessment for large and medium-sized taxpayers and setting up three federal tax offices in major cities in the South.

19. **Fiscal decentralization.** Pro-poor spending (i.e. transfers to states, state-level capital expenditures and some pro-poor national development expenditures) increased in 2005 and is expected to increase further in 2006. In order for such spending to realize the intended benefits, a strengthening of public financial management at all levels of government (including better transparency and accountability) is our key priority. We also plan to make significant progress on the public expenditure review, which will focus on pro-poor spending, decentralization and public financial management, and implement the necessary provisions to ensure coordination in budget preparation, execution, and monitoring between the national government, the GOSS, and other states. To underpin the decentralization reforms envisaged under the CPA and to maximize the benefit from cooperation among the different levels of government, rules and procedures for the Fiscal and Financial Allocation and Monitoring Commission will be established and made operational by end-June 2006.

20. **Fiscal reporting and accounting.** We are committed to the implementation of GFS methodology at all levels of government. We will begin reporting under the GFS format the 2006 fiscal framework of the national government to parliament (by May) and monthly budget execution (by June). The GOSS is also committed to fiscal transparency and regular reporting and will follow the same schedule as the National Government. Other aspects of GFS implementation will require a larger project to support public financial management at the national, state and local levels, for which we will seek assistance from development partners. We also intend to upgrade our system of recording the outturn of development spending from the current cash basis to an accrual basis. The current system, among other difficulties, has led to inaccuracies in the measurement of development spending and in a pattern of accumulation of arrears that are paid down in the subsequent year. Later this year, we will modify the chart of accounts to ensure that the 2007 budget is prepared in accordance with GFSM 2001.

21. **Oil revenue management and transparency.** As the oil sector becomes more important in Sudan's economy, we will ensure that oil proceeds are wisely used for the welfare of the whole population. Our response to the specter of the "oil curse" in the form of wasteful use of oil revenues that have affected a number of countries with dire consequences for development will be transparency in oil sector operations and sound expenditure policies. In the near term, we will publish monthly detailed oil sector data and clarify the role and status of the National Petroleum Commission consistent with the CPA. We will also publish the 2004 and 2005 audited accounts of Sudapet, and ensure regular transfers to the treasury of the net operating income from the Sudan Petroleum Corporation and from Sudapet including that resulting from exports of fuel products. In addition, the

prevailing marketing mechanism (open international tenders) for export of Nile blend crude will be extended to the new Dar blend crude after an initial test period of six months. Lastly, we intend to discuss will be discussing with Fund staff the medium-term agenda for subsequent oil sector reforms, including the process for joining the Extractive Industries Transparency Initiative.

22. **Financial sector.** In 2006, we will implement restructuring plans for the central bank and for commercial banks as well as the financial reform program discussed during the recent FSAP. We are also planning to introduce the new national currency (as envisaged in the CPA) in the second half of this year. We have also initiated a reform program to develop and restructure commercial banks (2006-2008). By end-2006, we will increase minimum capital requirements for commercial banks from SDD3 billion to SDD6 billion (US\$25 million) and increase the capital adequacy ratio from 8 to 12 percent. We will also require banks to implement action plans to meet provisioning and capitalization requirements. Lastly, the CBOS will encourage mergers of commercial banks according to specific guidelines. In order to permit screening of any merger/acquisition, we will carry out an evaluation of banks to identify their net worth and share value.

23. **Trade and Payments.** In the 2006 budget, we initiated the first phase of the three-year tariff reform program by reducing the top tariff rate from 45 percent to 40 percent, which will reduce the average tariff rate to 20 percent. By 2008, we plan to further reduce tariff dispersion and lower the average tariff rate below 15 percent, especially through reductions in the top tariff rate.

24. **Technical assistance.** For the coming year, we would like to request further technical assistance from the Fund and other development partners in the following key areas:

- Implementation of Government Finance Statistics Methodology (GFSM 2001) (budget classification, accounting, execution, and auditing)
- Budget reporting, including accounting of development expenditures
- Fiscal decentralization and public financial management
- Issuance of the new currency
- Banking supervision
- Liquidity management
- Microfinance
- Balance of payments, monetary, and real sector statistics.

IV. RELATIONS WITH THE FUND AND OTHER CREDITORS

25. **External debt problems.** In 2006, Sudan's debt service payments capacity will be constrained by the considerable burden of implementing the peace agreement and dealing with widespread poverty and regional inequalities. Any shortfall (or even a delay) in donor assistance or a significant negative shock in oil prices would further limit our capacity to service our obligations. We are making partial debt service payments to almost all multilateral creditors and selected bilateral creditors that have provided new financing in recent years. At the end-2005, stock of public and publicly guaranteed external debt was about US\$27.7 billion in nominal terms, of which US\$24.4 billion was in arrears. We are still hopeful for an early resolution of Sudan's debt problems—including debt relief under the HIPC initiative and under the Multilateral Debt Relief Initiative—through concrete action by our key creditors and multilateral institutions. Needless to say, Sudan's income level calls for substantial debt relief to finance programs for achieving the Millennium Development Goals.

26. **External financing.** Sudan has continued to suffer from limited access to concessional loans because of the difficulties in resolving our debt and arrears situation. Development needs, however, are vast, and we have had to rely on nonconcessional facilities to finance critical development and social projects. We are fully aware of the concern of other creditors about this borrowing, and we will limit the contracting of such facilities as much as possible. At the same time, we see these levels of borrowing as exceptional and temporary, as they are an integral part of our strategy to unite the country after the signing of the peace agreement with the South. For this year, we will need to begin critical infrastructure and transportation projects that will require new financing equivalent to as much as US\$700 million. Two critical large projects involve the reconstruction of a railway linking the North and the South and the construction of roads to the South and to Darfur. We will make every effort to avoid incurring nonconcessional loans and we hope that we can obtain concessional resources from donors and other creditors. At the same time, these projects cannot wait, and this may force us to contract nonconcessional loans for up to that amount. In line with our commitment to increase the transparency of public sector operations, we will continue to share openly with Fund staff our plans and information on loans and we will publish detailed information on all government or government guaranteed facilities (see Table 2 below).

27. **Payments to the Fund.** In addition to strong cooperation with the Fund on economic policy matters, Sudan made regular payments to the Fund as committed under the 2005 SMP. The Fund's preferred creditor status will be maintained by ensuring that our payments continue to exceed obligations falling due. To demonstrate our continued cooperation, we will increase payments to the Fund from US\$30 million in 2005 to US\$45 million in 2006. However, because oil and non-oil revenues will be much lower in the first half of the year (the new oil fields will only be at full production in the second half of the year and non-oil revenues are cyclical), payments to the Fund up until June will be

US\$15 million. We hope that our record of cooperation will be fully recognized at the appropriate time through a rapid resolution of Sudan's debt and arrears problems.

V. PROGRAM TARGETS AND MONITORING

28. **Program monitoring.** The program covers the period January-December 2006 and takes into account the financial position of the South. It contains semi-annual quantitative targets (end-June and end-December test dates) and structural benchmarks. Given the impact of the South's finances for the financial program, the targets on net domestic assets and international reserves of the central bank will have an adjustor for any lower-than-programmed withdrawals of deposits by the government of South Sudan as noted in the attached Technical Memorandum of Understanding (TMU). There is also an adjustor on the value of oil export proceeds. The program targets and key structural benchmarks are specified in Tables 1 and 2 below.

29. **Compilation and provision of information.** To insure the effective monitoring of the program, the relevant ministries, the CBOS, and the Central Bureau of Statistics will compile and share with Fund staff all core economic data on a timely basis as specified in the attached TMU.

Table 1. Sudan: Quantitative Targets Under the Staff-Monitored Program 1/

	2005 2/ Dec.	Cumulative Change During 2006			
	Actual	Jan.-March Indicative	Jan.-June Mid-year Program	Jan.-Sept. Indicative	Jan.-Dec. End-year Program
(In billions of Sudanese dinars; unless otherwise indicated)					
Central Bank of Sudan net domestic assets	76.1	41.8	21.2	13.9	-5.0
Domestic financing of the central government	109.6	48.7	36.9	6.8	21.1
Net international reserves	1,889	53	283	451	700
Contracting or guaranteeing of external nonconcessional debt by the government or the central bank (in millions of U.S. dollars)	935	...	...	...	700
Payments to the Fund (in millions of U.S. dollars)	30.3	...	15.0	...	45.0
Memorandum items:					
Broad money	1,403	74	151	248	393
Reserve money	612	57	88	119	153
Programmed oil export revenues to the government	...	157	382	637	889
<i>Of which:</i> oil savings account	64	26	57	87	114

Sources: Sudanese authorities; and Fund staff estimates.

1/ As specified by the technical memorandum of understanding.

2/ Outstanding stock at end-2005.

Table 2. Structural Measures for 2006

Measures	Timing (end of period)
<i>Prior Actions</i>	
Stop the referral of requests for renewal of exemptions under the Investment Encouragement Act by the Minister of Investment to the Council of Ministers	Throughout after March 2006
<i>Other Measures</i>	
Convert the 2006 fiscal framework of the National Government to GFSM 2001 classification and present it to parliament for information (including the economic and functional classification of expenditures)	May 2006
Finalize and publish GOSS budget reporting for 2006 according to GFSM methodology (economic and functional classification)	May 2006
Initiate a public information campaign sensitizing the public about the costs of fuel subsidies and highlighting pro-poor policies of the government	June 2006
Compile (monthly) and publish (quarterly) fiscal reporting data according to GFSM 2001 for the national government and the GOSS (economic and functional classifications).	June 2006
Issue a decree establishing the rules and procedures for the operations of the Fiscal and Financial Allocation and Monitoring Commission (FFAMC)	June 2006
Begin monthly publication on the Sudan Petroleum Corporation (SPC) and the central bank websites of the following information (one-month lag) (i) volume of oil production by blend of crude; export receipts and prices (in US\$) by blend, sales to refineries, exports and imports of petroleum products, revenue accrued to the government, and transfers to the government of Southern Sudan; and (ii) details of any new external loan or financing contracted or guaranteed by the government or the central bank, specifying the nature of the contract and the amount and terms.	July 2006
Complete and publish the 2004 and 2005 financial audits of Sudapet	September 2006
Finalize a strategy for the elimination of fuel subsidies and the adoption of an automatic mechanism that passes through changes in the world price of crude oil to domestic product prices.	October 2006
Finalize a program to revamp the system of investment incentives granted under the Investment Encouragement Act and in line with best international practice.	October 2006
Remit net operating income of Sudapet (at year end) and the SPC (quarterly), including those derived from exports of petroleum products to the treasury	Throughout

SUDAN
TECHNICAL MEMORANDUM OF UNDERSTANDING

1. This memorandum specifies the understanding reached with the Fund staff regarding quantitative targets, structural benchmarks, and reporting for the 2006 staff-monitored program (SMP).

2. The SMP relies on five quantitative indicative targets for up to end-March and end-September and an equal number of quantitative targets for end-June and end-December. The targets are (i) ceilings on the change in net domestic assets of the Central Bank of Sudan (CBOS); (ii) ceilings on the domestic financing of the fiscal deficit; (iii) floors for the buildup of net international reserves of the central bank; (iv) ceilings on new nonconcessional external loans contracted or guaranteed by the government or the central bank; and (v) floors for payments to the Fund. Broad money, reserve money, total government revenues from crude oil exports and oil savings account will be monitored as memorandum items. Some of these targets are subject to adjustors depending on the financial position of the government of South Sudan and total government oil export revenue performance. The definitions of these variables and the adjustors are set out below. All the quantitative targets and structural benchmarks are displayed in Tables 1 and 2 of this attachment.

3. **Net domestic assets (NDA)** of the CBOS are defined as the sum of the Net Domestic Credit of the CBOS, the net issue of money market instruments and other items net. Net Domestic Credit is defined as net credit to the central government (i.e. Government Musharaka Certificates (GMCs), Government Investment Certificates (GICs), and any other form of central bank credit to the central government minus total central government deposits) plus net central bank claims on state and local governments, central bank claims on public enterprises, and claims on banks, and minus Central Bank Ijara Certificates (CICs). The definition of the central government comprises all accounts of line ministries and agencies controlled by the government (corresponding to Group no. 11, Group no. 12, and some accounts of the Group no. 19 in the CBOS general ledger), the Zakat funds (recorded under Group no. 13), and margin deposits placed with the CBOS by the central government against letters of credit issued by the CBOS. The definition includes all oil-related accounts controlled by the government. To evaluate program targets, the dinar equivalent values of foreign exchange denominated items in the balance sheet of the central bank will be calculated at the program exchange rate.

4. **Domestic financing of the fiscal deficit** is defined as total net domestic borrowing by the central government, including net borrowing from the banking system (including GMCs and GICs), net sales of GMCs and GICs outside the banking system, and revenues from privatization. The definition of central government for the purpose of this criterion is the same as the one applied for the NDA of the central bank.

5. **Net international reserves (NIR)** are total gross non-earmarked official foreign reserve assets on active accounts plus reserve assets of the government of Southern Sudan in the central bank minus official short-term liabilities (i.e. no more than one-year maturity). The assets are maintained on accounts with overseas correspondent banks and foreign exchange banknotes in the vaults of the central bank. Short-term liabilities include short-term liabilities, IMF deposit accounts, nonresident deposits, and (overdrawn) foreign correspondents accounts.

6. Limits on **contracting or guaranteeing of nonconcessional external debt** apply to all forms of debt of more than one-year maturity contracted or guaranteed by the government or the CBOS. It applies not only to debt as defined in point no. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision no. 12274-(00/85), August 24, 2000), but also to commitments contracted or guaranteed for which value has not been received. The degree of concessionality of debt will be calculated as specified in the Guidelines.²

7. **Broad money** is defined as the sum of local currency circulating outside of the banks, banks' demand, and time and savings deposits. It also includes transferable deposits and margin deposits against letters of credit placed by state and local governments, nonfinancial public enterprises, and the nonbank private sector with the CBOS. **Reserve money** is defined as the sum of local currency circulating outside of the banks, total reserves (required and excess) for banks, and deposits at the CBOS included in broad money.

8. **Adjustor on the financial position of the government of South Sudan** (capped). The program target for changes in the NDA of the central bank will be reduced (increased) and the international reserve target will be increased (reduced) by the amount of any decline (increase) in net central bank claims on the government of South Sudan. The adjustor will not apply if the stock of net claims on the government of South Sudan turns positive.

9. **Oil revenue adjustor** (symmetric). The programmed government oil revenue from crude oil exports is based on the program's assumptions about oil prices (f.o.b. Port Sudan) and quantities expected to be exported (see Table below). Accrued revenue is the cumulative government oil revenue inflows based on actual shipments at current international prices (f.o.b. Port Sudan). The portion of oil revenue for use in the 2006 budget is estimated at a price of oil of US\$45 per barrel for Nile blend and US\$40 for Dar blend (benchmark prices). The accrued government oil revenue in excess of the planned budgeted amounts is deposited

² For program purposes, a loan is considered concessional if the grant element is at least 35 percent calculated using a discount factor based on the Commercial Interest Reference Rates (CIRRs) published by the OECD plus margins depending on the loan maturity. The margins are 0.75 percent for repayment periods of less than 15 years, 1 percent for 15–19 years, 1.15 percent for 20–29 years, and 1.25 percent for 30 years or more. The average of the CIRRs over the last ten years will be used for loans with a maturity of at least 15 years and the average of the CIRRs for the preceding six months will be used for shorter maturities.

in an oil saving account (OSA), a locked sub-account within net credit to the government at the CBOS. The programmed OSA accumulation for the year is US\$509 million.

The oil revenue adjustor will work as follows:

- If the accrued government revenue from crude oil exports exceeds the programmed amount (either because the price and/or volume exceed the programmed levels), these proceeds will also be deposited in the OSA. The program targets for domestic financing of the budget deficit and NDA will be reduced, and the international reserves target will be increased, by the difference between the accrued and the programmed amounts.
- If the accrued government revenue from crude oil exports falls short of the programmed amount, the program targets for domestic financing of the budget deficit and NDA will be increased and the international reserves target will be reduced by the difference between the programmed and the accrued amounts.
- If within a given quarter the accrued oil revenue that goes to the budget falls below the planned amount, appropriate amounts will be withdrawn from the OSA to ensure that cumulative oil revenues for use in the budget match the cumulative amounts planned in the fiscal program.

Table 1. Sudan: Government oil revenues from crude exports

		2006				
		Q1	Q2	Q3	Q4	Year
Nile blend crude						
Price (f.o.b. Port Sudan)	US\$/barrel	53.9	55.2	55.1	54.7	54.7
Volume exported	Million barrels	12.9	13.5	13.5	12.4	52.2
Export revenues	US\$ millions	698	745	741	676	2,859
<i>Of which:</i> programmed OSA accumulation	US\$ millions	116	138	136	119	509
Dar blend crude and block 5A crude						
Price (f.o.b. Port Sudan)	US\$/barrel	40.0	39.5	39.4	38.9	39.5
Volume exported	Million barrels	0.0	6.4	10.0	11.5	27.9
Export revenues	US\$ millions	0	254	393	447	1,094
<i>Of which:</i> programmed OSA accumulation	US\$ millions	0.0	0.0	0.0	0.0	0.0
Memo item:						
Programmed revenue from crude exports	US\$ millions	698	999	1,134	1,122	3,953
Programmed revenue from crude exports	SDD billions	157	225	255	253	889
<i>Of which:</i> programmed OSA accumulation	SDD billions	26	31	31	27	114
Planned oil export revenue for the budget	SDD billions	131	194	225	226	775

10. **Data Reporting.** The following table contains the agreed reporting framework. To the extent possible, the data will be submitted in both printed and electronic form to the IMF local office.

Reporting Agency	Type of Data	Description of Data	Frequency	Timing (within period specified)
CBOS	Flash report	Weekly data for movement in main indicators of the CBOS balance sheet, international reserves, sales and purchases of foreign exchange, exchange rate, murabaha rate, musharaka shares, and inflation	Weekly	Tuesday of each week
	CBOS balance sheet	Detailed CBOS balance sheet.	Monthly	1 month after the end of each month
	Monetary survey	Banking system balance sheet and consolidated balance sheet of commercial banks	Monthly	1 month after the end of each month
	Rates of return and securities	Murabaha rate and shares of Musharaka and the rate of return on securities (GMC, GIC and CIC). Information on auctions and expiry for all certificates from the Sudan Financial Company	Monthly	1 week after the end of each month
	Banking indicators	Capital adequacy; asset composition and quality; profitability; liquidity; open FX positions; and compliance with prudential norms	Quarterly	1 month after the end of each quarter
	Balance of payments	Detailed composition	Quarterly	2 months after the end of each quarter
Ministry of Finance	Central government	Revenues, expenditures, and financing as in traditional presentation	Monthly	30 days after the end of each month
	Central government	Revenues, expenditures, and financing as in GFSM 2001	Monthly	Data for January-May by end-June, for the remaining months 45 days after the end of each month
	GOSS	GFSM 2001	Monthly	Data for January-May by end-June, for the remaining months 45 days after the end of each month
	Privatization receipts	Detailed figures for each transaction and nature of the transaction	Quarterly	1 month after the end of each quarter
	Bank financing	Certificates or advances from the central bank or commercial banks, listed by transaction specifying entity, date, amount, and maturity	Monthly	1 month after the end of each month
	Nonbank financing	Certificates or IOUs issued to any nonbank entity, listing by transaction specifying entity, date, amount and maturity	Monthly	1 month after the end of each month
	External debt	Disbursements, debt service, and contracting or guaranteeing of medium-and long-term external debt of the government, the CBOS, and state-owned companies	Quarterly	1 month after the end of each quarter
Central Bureau of Statistics	CPI	By category and income group (low, middle, high)	Monthly	1 week after the end of each month
Ministry of Finance/ Ministry of Energy	Crude oil exports	Shipment data, listing by blend specifying date, quantity, prices, and values in US\$ and in dinars	Monthly	1 month after the end of each month
	Sales to refineries	Sales listing by refineries specifying date, quantity, prices, and values in US\$ and in dinars	Monthly	1 month after the end of each month
	Net operating income transfers to the treasury	Net income of SPC (including those derived from exports of petroleum products)	Quarterly	1 month after the end of each quarter

**Statement by the IMF Staff Representative
May 3, 2006**

1. The following information has become available since the issuance of the staff report on November 7. It does not change the thrust of the staff appraisal.
2. The staff and the authorities discussed the issue of nonconcessional borrowing within the 2006 Staff-Monitored Program (SMP) during the Spring Meetings. The authorities are aware of Paris Club creditors' concerns about this type of borrowing and indicated that they would approach their other creditors to seek concessional terms with a view to minimizing nonconcessional borrowing in 2006. Furthermore, if the higher-than-projected oil price environment continues, the authorities will also look into the possibility of using additional oil revenues to substitute for the intended borrowing. The authorities also noted that the peace negotiations in Abuja are at an advanced stage, and they hope that Sudan's creditors will be ready to begin exploring financing options to resolve Sudan's debt and arrears problems after a peace agreement on Darfur is signed.
3. The staff urged the authorities to find some combination of additional oil revenue and concessional financing in order to minimize nonconcessional borrowing and thus address the concern about this borrowing raised in the staff appraisal (paragraph 49). In this regard, a final assessment of the program's strength will need to take into account actual developments, including in nonconcessional borrowing.
4. The authorities have given their consent to the publication of the staff report including the letter of intent, the Memorandum of Economic Policies, and the technical Memorandum of Understanding.



INTERNATIONAL MONETARY FUND

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May 24, 2006

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

IMF Executive Board Concludes 2006 Article IV Consultation with Sudan

On May 3, 2006, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Sudan.¹

Background

Despite some delays, the implementation of the Comprehensive Peace Agreement with the South began in 2005. An interim national constitution was put into force, the Government of National Unity and the government of Southern Sudan were set up, and the central government began transferring oil revenues to the South as stipulated in the peace agreement. Further work is required, especially to make operational the commissions envisaged in the agreement.

Sudan's economy has been growing at a fast pace and macroeconomic conditions have been stable. Real GDP grew at an estimated rate of 8 percent in 2005, owing mainly to a recovery in agriculture and robust activity in construction and services. After rapid growth in 2003 and 2004, oil sector output remained virtually unchanged in 2005, while average inflation was 8.5 percent.

The external current account worsened in 2005 but the balance of payments was supported by strong capital inflows. Oil export revenues rose because of higher oil prices, but imports rose drastically and non-oil exports slowed (owing to transportation bottlenecks, high domestic demand, and to some extent, real exchange rate appreciation). A continuation in the strong trend in capital inflows—primarily foreign direct investment in non-oil sectors—allowed for a buildup of international reserves from 1.9 months of imports at end-2004 to 2.6 months at end-2005.

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.

The central government fiscal balance turned to a deficit after three years of surpluses. Oil revenue continued to rise in 2005, but it could not keep pace with the increase in government spending, driven by higher transfers to subnational governments (including transfers to the South) and a large subsidy on domestic fuels. The subsidy is a significant drain on public resources without any direct benefit to the poor in Sudan.

In 2005, monetary growth remained high and the dinar appreciated. Money demand was bolstered by strong economic growth and further monetization, while the fiscal expansion, higher oil exports, and strong capital inflows contributed to an appreciation of the dinar.

The authorities took steps to improve the tariff structure and increase flexibility in the foreign exchange market. As part of a three-year import-tariff reform program, the top tariff rate was lowered from 45 percent to 40 percent, the average tariff rate fell to 20 percent, and is likely to decline further to 15 percent or less in the next two years. The authorities removed the remaining exchange restrictions under Article VIII of the Fund's Articles of Agreement and allowed for further flexibility (through auctions) in the pricing of foreign exchange. Sudan maintains a managed floating exchange rate regime.

There was progress on structural reforms in the fiscal and financial sectors, but more remains to be done. A medium taxpayer unit was set up to boost non-oil revenue. The adoption of Automated System of Customs Data system should improve efficiency at customs ports. Regarding financial reforms, the central bank introduced competitive auctions of government securities, privatized a large bank, and began to implement the financial reforms envisaged in the peace agreement with the South. Notwithstanding the progress made, more remains to be done to modernize the tax and the financial system, strengthen expenditure management at all levels of government, and improve fiscal and oil sector transparency.

Executive Board Assessment

Executive Directors commended the Sudanese authorities for pursuing prudent macroeconomic policies in recent years and carrying out structural reforms in a very difficult environment. These policies have resulted in a favorable economic performance marked by higher levels of foreign investment, robust economic growth, a strengthening of the external position, and single-digit inflation. Directors urged the authorities to continue implementing sound economic policies and to persevere with the structural reform agenda.

Directors noted the challenges that the authorities face in mobilizing and transferring resources to meet the requirements arising from the implementation of the Comprehensive Peace Agreement, reconstruction, and national unification, as well as in dealing with profound regional tensions and disparities. In this regard, Directors stressed the need to ensure the effective operations of the North-South commissions and resolve the crisis in Darfur in order for Sudan to realize its full economic potential. This will also set the stage for moving towards the Millennium Development Goals, which will also require the full support of the international community.

Directors considered that performance under the 2005 Staff-Monitored Program (SMP) was broadly satisfactory. In particular, they welcomed the policy actions to contain inflation and the implementation of most structural benchmarks under the program. Directors regretted, however, the higher-than-programmed level of nonconcessional borrowing and the delay in setting up the framework for fiscal reporting according to Government Finance Statistics methodology.

Directors broadly endorsed the policy package embedded in the 2006 SMP but urged the authorities to minimize nonconcessional borrowing. They commended the authorities for their commitment to carry out prudent monetary and fiscal policies and proceed with fiscal reform priorities. Directors particularly welcomed the measures to increase transparency in oil sector operations, including the monthly publication of detailed oil sector data, and encouraged the authorities to join the Extractive Industries Transparency Initiative. Directors also welcomed the authorities' decision to increase the level of payments to the Fund, despite severe financial constraints. However, some Directors called for a further increase in line with Sudan's increased repayment capacity.

Directors acknowledged the recent improvements in monetary management and the central bank's intention to focus on its reserve money targets and to broaden the range of monetary instruments for a dual (Islamic and conventional) banking system. They saw substantial merit in maintaining exchange rate flexibility within the current managed float regime, while remaining vigilant to achieve the program's inflation objectives and undertaking reforms to enhance the business environment. In addition, Directors noted that close policy coordination between the central bank and central and subnational governments would be required to maintain price stability.

Directors considered the recent implementation of financial system provisions contained in the peace agreement with the South to be commendable. They encouraged the central bank to proceed with the reform agenda, especially the implementation of FSAP recommendations including the increase in minimum capital requirements. Directors also urged the authorities to embark on a well-planned and transparent process to introduce the new currency, a key step to foster development in the South and to integrate Sudan's economy.

Directors underscored the importance of pressing ahead with fiscal reform priorities. Investment incentives and other tax exemptions need to be rationalized in line with best international practice. These policies will ensure a level playing field, improve governance, and protect non-oil tax revenues. Another priority is to reduce fuel subsidies in order to alleviate economic distortions and preserve fiscal sustainability. In this regard, Directors were encouraged by the authorities' intention to carry out a public information campaign about the subsidies and develop an automatic mechanism for future price adjustments in line with changes in world oil prices. Directors encouraged the authorities to further reduce and ultimately eliminate the fuel subsidies, while, in this context, a few Directors also noted that the authorities will have to take into account the realities of such a process as they move forward.

Directors commended the authorities for the pro-poor focus of the 2006 budget framework,

including the higher transfers to the South and Northern states and higher capital expenditures. To address capacity constraints and improve transparency, especially in subnational governments, they stressed the need to move expeditiously to improve expenditure management systems, including through appropriate regulations, effective monitoring, and transparent reporting. Furthermore, Directors urged the authorities to begin compiling budget execution reports according to Government Finance Statistics methodology for both the Government of National Unity and the Government of Southern Sudan.

Directors urged the authorities to minimize the level of nonconcessional borrowing in 2006 in view of Sudan's already unsustainable external debt burden and in order to avoid complications in a potential debt relief operation. While acknowledging the country's reconstruction and unification needs, the larger transfers to the South and other states, and the need for higher social spending in order to make progress toward the Millennium Development Goals. Directors urged the authorities to use any windfall oil revenues to finance intended infrastructure projects or to seek concessional terms for any loan facility, and they supported their efforts in this regard. Many Directors underscored that all creditors have a responsibility in helping to ensure that Sudan's unsustainable debt is not aggravated further. They also pointed out that all creditors should participate fully and on equal terms in any debt restructuring and the HIPC Initiative for Sudan, and that the authorities should treat all creditors equally. Directors underscored the importance of tracking nonconcessional borrowing—both actual and planned—and called for close cooperation and exchange of information among all creditors.

A number of Directors called for a zero ceiling on nonconcessional borrowing in 2006, and could not support the inclusion of a ceiling of \$700 million in such borrowing in the SMP. In light of this level of nonconcessional borrowing, these Directors did not consider the 2006 SMP equivalent in strength to a Right Accumulations Program (RAP) that could contribute to Sudan's efforts to build a track record. Many other Directors, however, felt that a zero ceiling on nonconcessional borrowing would not be realistic given Sudan's exceptional circumstances. Some of these Directors viewed the 2006 SMP as equivalent to a RAP in all respects except for the level of nonconcessional borrowing, while others considered that all the policy commitments under the 2006 SMP continue to be in line with what would be required for a RAP. A number of Directors felt that Sudan's performance under the successive SMPs should be reflected in the timetable for arrears clearance, and emphasized the importance of presenting a timely and clear road map in this respect. Stressing the need for a continued constructive engagement with Sudan, most Directors felt that a final evaluation of performance under the SMP should take into account actual developments, including in the evolution of nonconcessional borrowing. They urged the authorities to continue to work, in close cooperation with staff, towards ambitious measures that would substantially reduce the level of nonconcessional borrowing.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case. The [Staff Report](#) for the 2006 Article IV Consultation with Sudan is also available.

Sudan: Selected Economic Indicators, 2001-2005

	2001	2002	2003	2004	2005
Real Sector					
Real GDP growth (percent change)	6.1	6.4	5.6	5.2	8.0
GDP (in billions of dinars)	3,454	3,978	4,614	5,573	6,748
GDP (in millions of U.S. dollars)	13,369	15,109	17,680	21,610	27,699
GNP per capita	374	425	486	579	790
Inflation (in percent)					
Period average	4.9	8.3	7.7	8.4	8.5
End-of-period	7.4	8.3	8.3	7.3	5.6
Central government operations (in percent of GDP)					
Revenue and grants	10.7	11.8	16.1	19.8	21.8
Expenditure	11.6	8.7	15.4	18.3	23.6
Overall balance (commitment basis)	-0.9	3.1	0.7	1.5	-1.8
Monetary Indicators					
Reserve money (end-of-period growth rate, in percent)	3.7	22.0	26.6	27.8	34.9
Broad money (end-of-period growth rate, in percent)	24.7	30.3	30.3	32.1	44.7
Broad money velocity	8.1	7.1	6.6	5.7	4.8
External Sector					
Current account balance (including transfers)	-1,257	-918	-827	-816	-2,341
In percent of GDP	-9.4	-6.1	-4.7	-3.8	-8.5
External debt					
In billions of U.S. dollars	20.9	23.6	25.7	26.0	27.7
In percent of GDP	157	156	145	120	100
Net international reserves (in millions of U.S. dollars)	-109	84	290	1,144	1,889
In months of next year's imports of goods and services	-0.5	0.3	0.8	1.9	2.6

Sources: Sudanese authorities; and IMF staff estimates.

**Statement by Peter Ngumbullu, Executive Director for Sudan
and John Steytler, Senior Advisor to Executive Director
May 3, 2006**

Key Points

- *Despite some initial delays due to various factors, including the untimely death of the First Vice President, John Garang, implementation of the CPA is on track and the payments of oil revenue to the Government Of Southern Sudan (GOSS) had been effected in line with the wealth sharing provision of the CPA. Implementation of other key elements of the CPA are also on track. However, lack of donor inflows is posing a challenge to the overall implementation of the peace agreement.*
- *The Authorities are working hard towards reaching agreement with all concerned parties along the lines of the CPA, regarding the situation in Darfur. They request the Fund to play a visible role and act as a full partner in the planned Joint Assessment Mission (JAM), comprising the World Bank, Africa Development Bank, and UN agencies which will assess and determine the post-conflict requirements of Darfur.*
- *In principle, the policy of the Sudanese authorities is not to contract non-concessional loans. The authorities request for special consideration since they do not have access to any form of concessional or development funding, and given the enormous needs of providing key social and physical infrastructure to make the peace attractive and to enhance the growth potential of the economy.*
- *The authorities are aware of the concern of Paris Club creditors about non-concessional borrowing. They will approach their other creditors to seek concessional terms with a view to minimizing non-concessional borrowing in 2006. Furthermore, if the environment of higher than projected oil prices persists, they will be exploring the possibility of using the additional oil revenues to substitute for the intended borrowing.*
- *After seven years of successful implementation of strong SMPs, the last four with policies equivalent in strength of Upper Credit Tranche conditionality, the authorities request that creditors and donors come up with a clear road map for Sudan on the way forward with respect to arrears clearance and debt relief under HIPC and MDRI.*

1. The Sudanese authorities appreciate the candid exchange of views during the 2006 Article IV Consultation and the Staff-Monitored Program discussions. They view the staff assessment as fair and balanced, and agree that there is a broad measure of agreement with staff on economic policies. The authorities would like to thank Management and the

Executive Board for their continued engagement and constructive policy advice and technical assistance provided to Sudan. They consent to publication of the staff report.

Progress on Implementation of the CPA and Darfur Negotiations

2. Despite a slow start and some initial delays due to various factors, including the untimely death of First Vice President, John Garang, implementation of the Comprehensive Peace Agreement (CPA) is on track. All commissions envisaged under the CPA had been established and transfer of oil revenues to the Government of South Sudan (GOSS), in line with the wealth sharing provision of the CPA, have started to take place. The Government of National Unity is trying its best to operationalize all the institutions of the CPA. Oil receipts have been verified by all parties concerned and there are no disputes on this matter. Implementation of other key elements of the CPA are also on track, such as the establishment of a central bank branch in Juba, issuing of rules and regulations on conventional banking for South Sudan and issuing of a new national currency with Fund TA. There are still some problems in the South with respect to budget preparation and execution due to capacity constraints and the authorities are requesting Fund TA to strengthen public expenditure management systems of the GOSS and states, in order to overcome this problem.

3. Following the last Board discussion on Sudan, the authorities have intensified their efforts to finding an amicable solution to the situation in Darfur. They expect to reach agreement soon along the lines of the CPA. A Joint Assessment Mission (JAM), comprising the World Bank, African Development Bank, Donor Community and UN agencies is planned, to conduct an assessment on the post-conflict requirements for Darfur, followed by a donor conference. It is expected that the JAM will focus on three key elements, namely, debt relief, development, and humanitarian needs. In this respect, the authorities request the Fund to play visible and pro-active role, in determining the post-conflict requirements of Darfur.

Recent Economic Developments and Prospects

4. Notwithstanding internal conflicts and the difficulties of concluding and implementing the CPA, Sudan's economic performance in recent years has been outstanding. Growth has been robust, inflation kept under control and a number of important reforms implemented. Furthermore, higher oil prices supported the balance of payments and allowed for further accumulation of reserves and appreciation of the Sudanese dinar against the U.S. dollar. So far, the appreciation of the currency has not led to loss of competitiveness, but the authorities are closely monitoring the situation. Going forward, economic growth is expected to be in the range of 8-10 percent in 2006, supported by a large increase in oil production and continued high growth in the non-oil sector; inflation is expected to remain at a low single digit level and reduction in poverty levels will be enhanced.

5. As staff note, a number of challenges and risks remain. The authorities remain vigilant and agree with staff on the need for prudent economic policies, to which they are fully committed. The authorities are aware of the enormous developmental challenges facing the country going forward, including full implementation of the CPA, tackling regional

inequalities and reducing poverty as well as avoidance of the “Dutch disease”. In this regard, they have launched a strategy to meet the Millennium Development Goals and will finalize their interim Poverty Eradication Strategy by the end of this year. The authorities will continue to reorient public spending towards less developed regions and social and infrastructure projects, as well as on capacity building and revamping of public financial management systems at all levels of government. They will need comprehensive and deep debt relief beyond the traditional mechanisms to clear arrears and achieve debt sustainability.

Fiscal Policy

6. The Authorities remain committed to implementation of prudent fiscal policies aimed at achieving fiscal and debt sustainability and restoring borrowing relations with the international community, including international financial institutions. In 2005, oil revenue was lower than programmed because of delay in commencing oil production in some oil blocks. In line with stipulations of the CPA, the authorities initiated transfers to the government of South Sudan.

7. In 2006, the fiscal deficit will be contained at below 1 percent of GDP. Oil revenue will increase because of higher international oil prices and estimated higher production, while non-oil revenue will benefit from improvements in administration, including collections in the South and other states, and from rationalization of tax exemptions. With respect to the latter, the Ministry of Investment will not refer to the Council of Ministers any proposal to renew expired business profit tax exemptions granted under the Investment Encouragement Act. By October 2006, the authorities will, in consultation with Fund staff, finalize a program to rationalize the system of investment incentives in line with international best practice. The authorities will also examine the scope for expanding the VAT base by bringing exempted items into the tax net.

8. On the expenditure side, the authorities will contain the intended increase in civil servant’s salaries, expenditure on goods and services, transfers to the northern states, and domestically financed capital expenditures to ensure that the fiscal framework is compatible with their goal of maintaining economic stability. Expenditure prioritization will be done in a manner to ensure spending on programs that directly benefit the poor is protected. The authorities hope that increased development assistance from the international community in 2006 will also help co-finance pro-poor programs. They agree that subsidization of domestic fuel prices is not sustainable. In this respect they prefer a phased reduction of fuel subsidies, starting in June this year by sensitizing Parliament and the public and ultimately adopt an automatic pricing mechanism in line with world market prices for petroleum products.

9. With regard to structural issues, the authorities are committed to further strengthen public expenditure management systems in 2006, implement the Government Finance Statistics Methodology (GFSM 2001), and enhance transparency in oil revenue management. Fiscal decentralization and improvement in fiscal reporting and accounting will also continue to be prioritized in the 2006 SMP. All measures to strengthen public expenditure management and enhance transparency are articulated in the authorities Memorandum of Economic and Financial Policies. These measures would, however, require a great deal of

Fund and World Bank Technical Assistance which the authorities hope they can continue to count on.

Monetary, Exchange Rate and Financial Sector Issues

10. The Sudanese Authorities remain committed to price stability through reserves management within the context of a flexible exchange rate system. High external inflows have recently led to an appreciation of the real exchange rate, but thus far there are no visible signs of tangible loss of competitiveness and overall the non-oil economy remains competitive. The authorities believe that for long-term prosperity, focus should be on improvements of total factor productivity for enhancing external competitiveness. Therefore, as these trends are expected to persist, the authorities will intensify efforts to improve the business climate for private sector participation, through removal of structural bottlenecks and other institutional reforms, as well as efforts to foster rural development.

11. With respect to financial sector reform, the authorities will implement restructuring plans for the central bank and commercial banks, as well as the financial reform program discussed during the recent FSAP. As envisaged in the CPA, a main central bank branch was established in South Sudan, rules and regulations were issued on conventional banking and a new national currency will be introduced in the whole country by June this year. The Bank of Sudan has also initiated a reform program to develop and restructure commercial banks during the period 2006-2009, with the first steps being an increase in the minimum capital requirement from SDD 3 billion to SDD 6 billion and an increase in the capital adequacy ratio from 8 to 12 percent by end-2006. Additional reforms include, the requirement of commercial banks to implement action plans to meet provisions and capitalization requirement and the encouragement of mergers of commercial banks according to specific guidelines.

Non-Concessional Borrowings

12. As a matter of policy, the Sudanese Authorities do not consider it prudent to borrow on non-concessional terms. They would refrain from such borrowing if they had access to concessional resources. They request that the special circumstances of Sudan be considered with respect to the conditionality on non-concessional loans. Currently, Sudan does not have access to any form of concessional or development funding from multilateral financial institutions, including the World Bank and the IMF and the African Development Bank. There is also a big shortfall from major bilateral donors. At the same time, there are enormous pressures to implement the CPA and provide key social services and physical infrastructure to sustain the peace and keep the country together and to enhance the long-term growth potential of the non-oil economy. In this respect, all non-concessional loans are directed to key projects, such as the North South Railway, the Darfur highway and provision of basic services such as hospitals, water and rural electrification. The authorities have been very transparent on the use of all non-concessional loans.

13. Nevertheless, to demonstrate their commitment to a strong program, the authorities together with staff, are exploring innovative ways to reduce the level of non-concessional

loans, including usage of any excess revenue from higher than projected oil prices and negotiation of concessional terms with key creditors. With these remedial actions, the authorities hope that Sudan will maintain RAP quality equivalence on all their policies so that they can move quickly to a formal successor program, arrears clearance and debt relief. In the meantime, they request the international community to provide concessional resources to enable them implement key social and physical infrastructure projects, that will make the peace dividend more tangible.

Technical Assistance

14. The Authorities are grateful for technical assistance being provided by various Fund departments. However, the challenges that Sudan face are enormous and have been further amplified by implementation of the CPA and the forthcoming agreement on Darfur, hence requiring additional TA. Under the CPA a number of new institutions had to be established at federal and state levels. The key challenge going forward would be to get these institutions operationalized, and this would require additional technical and financial assistance. Specifically the authorities request Fund TA in the following areas: implementation of Government Finance Statistics Methodology (GFSM 2001); budget reporting, fiscal decentralization and public financial management; issuance of the new national currency; banking supervision; liquidity management; microfinance and balance of payments, monetary and real sector statistics.

Roadmap/Way Forward

15. Sudan's end-2004 debt stock remains unsustainable and significantly above the HIPC threshold. In addition, Sudan needs substantial resources to finance post-conflict needs, including the development and reconstruction of Darfur. Indeed, to effectively reduce Sudan's debt burden, the country needs debt relief beyond traditional mechanisms and under the Enhanced HIPC Initiative and MDRI.

16. After seven years of successful implementation of high quality SMPs, with the last four being implemented to the level of Upper Credit Tranche conditionality, the authorities request that creditors and donors come up with a clear and timely road map for Sudan in terms of the way forward with respect to arrears clearance and debt relief under HIPC and MDRI. As discussed by the Board in December 2005, contributions from donors may need to constitute the bulk of resources needed to solve Sudan's debt and arrears problems. We, thus, request the creditors and donors to begin considering how to mobilize the necessary resources to address this issue.

17. We are still of the opinion that Sudan's strong track record of policy implementation under successive SMPs since 1999 should be adequate to justify a waiver of the RAP for arrears clearance, qualification for a successor program and speedy reach of the decision and completion points under the HIPC Initiative. Given the expiration of the sunset clause by the end of this year, we urge creditors and donors to move quickly in mobilizing the necessary resources to ensure that the protracted arrears cases will benefit from HIPC and MDRI debt

relief as soon as possible so that these countries make progress towards the achievement of the MDGs.

Conclusion

18. In conclusion, the authorities would like to reaffirm their strong commitment to prudent and market oriented policies aimed at growth, employment creation and poverty reduction. The authorities are aware that without peace, no development is possible, and therefore implementation of the CPA and peace in Darfur will remain centre stage in the authorities development strategy. Their task is, however, complicated by the high debt burden and lack of access to concessional and development finance resources. They trust that the Fund will continue to be fully responsive in providing technical assistance in the areas requested to build their capacity, strengthen the macroeconomic management and implement the reform agenda going forward. The authorities are looking forward to normalizing their financial relationship with the international community in the context of a formal arrangement with the Fund, instead of continuing with SMPs for an undetermined period of time. As proof to their commitment to normalize relations with creditors, the authorities have increased their payments to the Fund by 50 percent under the current SMP. We urge the international community to recognize and fully support the authorities' efforts by releasing concessional resources, including grant financing and removing sanctions to assist implementation of the CPA and the forthcoming Darfur peace agreement.