

LOAN COMMITTEE

January 21, 1986

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Minutes of Loan Committee Meeting to consider
MADAGASCAR - Agriculture Sector Operation
Held on December 23, 1985 in Conference Room E-1208

A. Present

Committee:

Messrs. **E. Stern** (SVPOP), Chairman
M. Qureshi
H. van der Tak
H. Scott
C. Michalopoulos
H. Wyss

Others:

Messrs. Wiehen
Elmendorf
Gulhati
Devaux
Meerman
Mmes. Marshall
Garcia-Zamor
Clements
Dubey
Rajapatirana
Imam
Peloscheck
Rigo
Artus (IMF)
Kimaro (IMF)

B. Issues

1. The meeting was called to consider a proposed Agricultural Sector Adjustment Credit for \$60 million. The discussion focussed on the issues outlined in the Country Policy Department's memorandum of December 18, 1985.

DISTRIBUTION

COMMITTEE

Senior Vice President, Operations (Chairman)
Senior Vice President, Finance
Vice President & General Counsel
Vice President, Operations Policy
Regional Vice President concerned*
Vice President, Energy & Industry (for lending
in these sectors and SALs)
Vice President, Economics and Research (for non-
project lending)

OTHERS

Standard (see OMS 9.25 page 7)

*Copy to all other Regional Vice Presidents

C. Discussion

Madagascar's Medium-term Prospects

2. In opening the discussion, several members of the Loan Committee enquired about Madagascar's medium-term economic prospects. The Region pointed out that the outlook for the next few years was severely constrained by the lack of foreign exchange and the heavy debt service burden. To achieve a rate of growth slightly above the rate of population increase would require a major effort by the Government to accelerate the adjustment process, and by the donor community. The donors and creditors would need to continue to provide substantial amounts of debt rescheduling and to increase disbursements by higher commitments, by shifting from project to program aid and by making a major effort to accelerate disbursements under ongoing projects, through project redesign if necessary. A macroeconomic scenario had just been completed by the September/October economic mission. For reasons of time it had not been included in the Loan Committee package, but it would be integrated with the other analyses in the final documents.

Government Objectives and Policies

3. The Chairman stated that the President's Report required further clarification of the measures already taken under the agricultural reform program. The Region indicated that this would be done in the final documents and that a draft agriculture development policy letter had now been received and would be attached to the President's Report following review during negotiations.

Rice Policy and Financing

4. Several members of the Loan Committee raised questions on the proposal for a rice buffer stock to be financed in part by IDA. The Region explained that the term "buffer stock" was a misnomer. The proposal was for the Government to define with the Bank a program of rice imports and to release these imports on the market in a counter cyclical fashion during the seasonal shortage period to reduce speculative behaviour. The Government will constitute a stock of rice which will be released and replenished according to automatic ground rules to be agreed upon by Government and the Bank. The role of the Bank will be to encourage the donor community to finance rice imports on concessional terms and to provide "last resort" finance that Government will be able to draw upon to replenish the stock. The Chairman indicated that the Bank should not provide financing for rice imports on a regular basis, and that the Bank should act only as the financier of last resort. He did not consider it appropriate to specify amounts of IDA financing available for potential rice imports, since this would depend on needs and circumstances and discourage financing from other sources. He also instructed the Region to include rice as a commodity for possible credit financing under the category of agricultural inputs.

Financing and Allocation

5. Several members of the Loan Committee questioned the procedures described for foreign exchange allocation and expressed concern that they may slow down disbursements. The Region explained that the proposed procedure was Open General License (OGL). Once an importer has been issued a license to import an item placed on OGL, he may be granted foreign exchange on a first-come first-served basis without limitation up to the amount of foreign exchange available under the credit. The Region indicated that the procedure had been introduced in Madagascar on the advice of the IMF to provide flexibility and felt it was appropriate, given the current administrative foreign exchange allocation system. The Chairman asked that the OGL categories be sufficiently wide as to ensure flexibility in the use of the foreign exchange provided under the credit. The Region indicated that the foreign exchange allocation system will be reviewed during negotiations with the objective of restoring the role of market forces despite the present foreign exchange shortage.

Exchange Rate

6. The adequacy of the exchange rate was questioned. The IMF representative indicated that Government had agreed to accelerate the depreciation of the exchange rate under the next Standby agreement. The Region indicated that the Malagasy authorities were ready to discuss the need for a major currency realignment.

Public Investment Program

7. The Chairman expressed concern about the Public Investment Program in agriculture and requested clarification on how the Region intended to deal with the "doubtful" projects. The Region explained that, as with in the Industrial Assistance Credit, Government will be requested to delay any expenditures or signing of contracts until studies have demonstrated the viability of the "doubtful" projects. The Chairman stated that the credit should only be presented to the Board when the Bank was satisfied with the investment program in agriculture.

Conditions of Effectiveness

8. Several members of the Loan Committee felt that too many conditions were set for Credit effectiveness, and therefore substantial delays could be expected before the Credit became effective. It was decided to reduce the number of conditions of effectiveness and convert

them, when appropriate, into specific covenants or conditions of Board presentation. Thus the following will be conditions for Board presentation:

- (1) a satisfactory agricultural PIP for 1986-1988;
- (2) adoption of a plan to eliminate progressively the 10% commission for parastatals exporting crops;
- (3) agreement on a calendar to reorganize the stabilization funds;
- (4) adoption of legislation to reduce the list of price control crops and agree on a pricing system for the crops whose prices would remain controlled;
- (5) adoption of incentive level paddy prices for 1986 in the two reserved areas;
- (6) agreement on a system to manage rice imports for 1986.

9. The Loan Committee agreed on a US\$ 60.0 million credit, of which US\$45.0 million would be allocated for agricultural inputs including the possibility of rice financing, US\$5.0 million for incentive goods and US\$10.0 million for transport equipment and spare parts.

D. Conclusion

10. The Region was authorized to negotiate the proposed credit on the terms and conditions approved by the Committee as reflected in the above discussion.