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REPORT AND RECOMMENDATION OF THE PRESIDENT OF THE INTERNATIONAL DEVELOPMENT ASSOCIATION TO THE EXECUTIVE DIRECTORS ON A PROPOSED DEVELOPMENT CREDIT IN AN AMOUNT EQUIVALENT TO SDR 35.3 MILLION TO THE REPUBLIC OF SENEGAL FOR A FINANCIAL SECTOR ADJUSTMENT PROGRAM

NOVEMBER 28, 1989

CURRENCY EQUIVALENTS

Currency Unit	=	CFA Franc (CFAF) 1/
US$ 1.00	=	CFAF 315.75 (November 1989) 2/
CFAF 1 million	=	US$ 3,167.06 (November 1989) 2/

SYSTEM OF WEIGHTS AND MEASURES: METRIC

Metric		U.S. Equivalent
1 meter (m)	=	3.28 feet (ft)
1 kilometer (km)	=	0.62 miles (mi)
1 square kilometer (km^2)	=	0.39 square mile (sq mi)
1 hectare (ha)	=	2.47 acres (a)
1 metric ton (t)	=	2,205 pounds (lb)
1 kilogram (kg)	=	2.2046 pounds (lb)

FISCAL YEAR

July 1 - June 30

1/ The CFA Franc is tied to the French Franc (FF) in the ratio of FF 1.0 to CFAF 50.0. The French Franc is currently floating.

2/ Exchange rate of November 14, 1989.

ABBREVIATIONS AND ACRONYMS

APB	Association professionelle des banques (Bankers' professional association)
BCEAO	Banque centrale des Etats de l'Afrique de l'Ouest (Central Bank of West African States)
BIAOS	Banque .nternationale pour l'Afrique occidentale - Sénégal (Commercial bank)
BNDS	Banque nationale de développement du Sénégal (National development bank of Senegal)
BICIS	Banque internationale pour le commerce et l'industrie du Sénégal (Commercial bank)
BSK	Banque sénégalo-koweitienne (Commercial bank)
CIDA	Canadian International Development Association
CCCE	Caisse centrale de coopération économique
CFA	Communauté financière africaine (African Financial Community)
CNCAS	Caisse nationale de crédit agricole du Sénégal (National Agricultural Credit Bank of Senegal)
ONCAD	Office national de coopération et d'assistance au développement (defunct groundnut marketing agency)
SME	Small and medium-scale enterprise
TEN	Taux d'escompte normal (normal rediscount rate)
TEP	Taux d'escompte préférentiel (preferential rediscount rate)
TES	Taux d'escompte (rediscount rate of last resort)
TMM	Taux du marché monétaire (money market rate)
UMOA	Union monétaire ouest-africaine (West African Monetary Union)
USAID	Unites States Agency for International Development
USB	Union sénégalaise des banques (Commercial bank)

REPUBLIC OF SENEGAL

FINANCIAL SECTOR ADJUSTMENT PROGRAM (FSECAL)

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REPUBLIC OF SENEGAL

FINANCIAL SECTOR ADJUSTMENT CREDIT

CREDIT SUMMARY

Borrower:	Government of Senegal
Credit Amount:	IDA: SDR 35.3 million (US$ 45.0 million equivalent)
Cofinancing:	France (US$34.0 million); United States (US$33.0 million).
Terms:	Standard IDA terms with a 40 years maturity.
Description:	The proposed Credit will support the efforts of the Government of Senegal to restructure its banking system and lay the groundwork for the development of well functioning financial and capital markets. It would take place within the framework of reforms by the West Africa Monetary Union (UMOA) of which Senegal is a member. These reforms follow intensive consultations between staff of the BCEAO (the common central bank of UMOA) and the Bank, the IMF, France and the US. They are noteworthy because they represent the consensus on a course of action toward financial sector reform by the seven members of the Union: Benin, Burkina, Cote d'Ivoire, Mali, Niger, Senegal and Togo.
Benefits and Risks:	The potential benefits of this Credit are substantial in that it not only would rehabilitate the Senegalese banking system but it would also establish an improved financial intermediation system that would aid in the mobilization and term-transformation of financial resources and in their channeling to borrowers hitherto largely excluded from access to credit. The risks associated with this adjustment credit are acceptable. The macroeconomic weaknesses that have undermined financial restructuring in other countries are unlikely to compromise the restructuring of Senegal's financial sector. SAL IV, whose preparation is now in its final stages, provides, in conjunction with the IMF's ESAF, for measures improving Senegal's fiscal and internal sector positions. Senegal's overall macro-economic stability is also reinforced by a central feature of the franc zone, which imposes strict and well-enforced limits on member-governments borrowing from the Central Bank.

<u>Estimated Disbursements</u>: The proposed credit would be disbursed in two tranches, the first becoming available on effectiveness (December 1989), the second nine months after disbursement of the first. In view of extensive reforms already undertaken, 60 percent of the credit (US$ 27.0 million) would be disbursed in the first tranche. Disbursement of the second tranche (US$ 18.0 million) would depend upon satisfactory overall implementation of the Program. Disbursements are expected to be made over a period of 12 months ending in December 1990.

<u>Map</u>: IBRD 18499R

<u>Appraisal Report</u>: There is no separate Staff Appraisal Report.

REPORT AND RECOMMENDATION OF THE PRESIDENT OF THE INTERNATIONAL DEVELOPMENT ASSOCIATION TO THE EXECUTIVE DIRECTORS ON A PROPOSED IDA CREDIT TO THE REPUBLIC OF SENEGAL FOR A FINANCIAL SECTOR ADJUSTMENT PROGRAM

1. I submit the following report and recommendation for a proposed credit to the Republic of Senegal to help finance a Financial Sector Adjustment Program (FSECAL). The proposed credit for SDR 35.3 million (US$45.0 million equivalent) would be on standard IDA terms with a maturity of 40 years.

PART I - THE ECONOMY

2. The latest Country Economic Memorandum entitled "Senegal: An Economy Under Adjustment" (No. 6454-SE) was distributed to the Executive Directors on February 13, 1987. Basic country data are given in Annex I.

A. Recent Developments

3. Adjustment of the Senegalese economy became unavoidable at the end of the 1970s, when a combination of poor financial and economic policies plunged an already weak economy into a severe crisis. A first attempt to stabilize the financial situation and create the basis for growth did not yield satisfactory results. Renewed efforts were launched in 1984 and resulted in the reduction of the fiscal deficit (from 5.8 percent of GDP in 1983/84 to 2.6 percent in 1987/88), the strengthening of the current account position (from 17.3 percent of GDP to 9.6 percent) and the dampening of the inflationary pressures (from 12 percent to 2.0 percent).

4. Adjustment efforts have also been accompanied by a revival of the economy. Between 1984 and 1988, real GDP grew by 4.3 percent annually as compared to long-term average growth rate of less than 2.5 percent in the preceding two decades. Growth has been driven principally by a good performance of the agricultural sector due to both favorable price incentives, particularly for groundnuts, which is the key cash crop, and to several years of good rainfall. As a result, the production of groundnuts and cereals has expanded at an annual rate of about 10 percent during the past four years. The fishing sector has also experienced significant growth and fish exports have become Senegal's largest export earner since 1985. There are, however, signs of resource depletion, particularly for the high-value pelagic fish species. While the recovery in groundnut production has stimulated the oil-processing industry, other manufacturing industries have remained depressed because of a combination of factors, including the poor investment climate, high cost of production factors (particularly labor and energy), a rigid labor market, and stiff competition from imports following the trade liberalization measures introduced since 1986. The service sector, which accounts for over half of GDP, has performed well in spite of the declining share of Government services. With domestic credit growing at an annual rate of 8.4 percent

since 1984 (about half of which was for crop credits), the domestic inflation rate has been modest, with the GDP deflator increasing at a rate slightly over two percent per annum.

5. With the population currently growing at 2.9 percent a year, higher GDP growth in the past few years has helped reverse the gradual decline in real per capita income which was experienced in the period 1960-84. Demand management measures implemented since 1984 have succeeded in reducing gross domestic expenditure, especially total consumption, which exceeded GDP during the first half of the eighties. As a result, domestic savings, which were negative in earlier years, recovered to reach 7 percent of GDP in 1988. Prudent demand management, which is crucial for avoiding real exchange rate appreciation under a fixed exchange rate regime, as well as a succession of good harvests, have contributed to the fall in the inflation rate which has enabled Senegal to regain some competitiveness in foreign markets. The country's exports continue to be impaired by the high cost of production in particular labor cost. Although growth in the level of nominal wages has been moderate, it still remains quite high by comparison to countries in the same GDP bracket as Senegal.

6. In spite of these improvements in the economic situation, the Government's fiscal situation remains fragile as evidenced by the significant shortfall in fiscal revenue in 1988/89. The combination of a weak economy and social disturbances related to the border conflict with Mauritania caused tax revenue to fall in nominal terms by 5 percent compared to the level in the preceding year and 13 percent compared to the projected l$el. The Government budget also relies heavily on the tax on petroleum products (about 25 percent of total revenue) whose domestic prices are 2.5 times world prices. Moreover, Senegal is still highly dependent on direct budgetary assistance from abroad to cover current expenses, including the servicing of foreign debt and the repayment of arrears. The excessive reliance on petroleum and external financing increases the vulnerability of the Government's financial operations vis-a-vis external developments. The debt service ratio of 25 percent in 1988 could be held to this level largely because of successive debt reschedulings by Paris Club members. Without reschedulings, the ratio would have exceeded 30 percent in that year.

B. Prospects and Financing Needs

7. The successful implementation of the FSECAL depends to a large extent on the macroeconomic stabilization program proposed under the SAL IV, currently in its last stages of preparation, and the ESAF of the IMF, which is in its second year of implementation. Both SAL IV and the ESAF contain specific policy measures aiming at the improvement of the fiscal situation and the current account position and providing for a prudent monetary policy. Assuming quick and full implementation of the policy reforms under the proposed SAL IV consistent with those spelled out by the Government in its fourth Policy Framework Paper to be discussed soon by the Committee of the Whole, the performance of the economy achieved in the recent past would be sustained. Real GDP growth, after registering a decline in 1989 to 1.3 percent would increase to an average of 3.8 percent over the period 1990-97, representing an increase of nearly 1 percent per

capita. Gross domestic investment, in particular private investment, would increase gradually and would be financed increasingly from domestic savings.

8. The overall fiscal situation, now in deficit, is projected to turn into a surplus by 1992, and then remain positive thereafter. This would be achieved through both containment of expenditure (reduction in nominal terms of the civil service wage bill and of transfers to parastatals) and improvement in resource mobilization (widening of the tax base, better tax administration, and higher across-the-board import duty rate). The current account position, which is projected to decrease by nearly half during the period 1990-97, would be strengthened through a further improvement in the export incentive system (i.e., reduction in the costs of production, in particular labor and energy, and elimination of administrative bottlenecks) and in the rationalization of public investment programming. The stabilization program contains also measures to limit the expansion in the domestic credit to 5 percent and to contain the inflation rate to less than 3 percent per annum.

9. The cumulative external capital requirements implied by this scenario during the period 1989-97 is projected at US$7.6 billion or about an average of US$ 840 million a year. This consists of US$4.5 billion of current account deficit (excluding transfers), US$ 2.4 billion of debt amortization (including IMF repurchases) and US$ 0.7 billion of changes in reserves. The proposed FSecal and SAL IV will meet part of these financing requirements. Nearly 30 percent of the identified financing would be in the form of official grants, consistent with the need to reduce the debt service burden. The unfilled gap is projected to average 15 percent of total financing requirements which is quite manageable given declining debt service levels.

PART II - THE FINANCIAL SECTOR

10. Senegal's banking system has become increasingly illiquid because of the accumulation of nonperforming loans now amounting to about US$750 million. These loans represent about half the portfolio of the banking system, or 13 percent of GNP. The absence of liquidity in much of the system hobbles the day-to-day functioning of commerce and industry and limits the access of potential borrowers to financing. It also affects the operations of the Treasury as taxpayers have increasingly been paying their taxes with checks drawn on frozen accounts in the illiquid banks. Financial intermediation, never well developed in Senegal, has been weakened by the growing inability of distressed banks to supply critical services and by the undermining of the country's financial transactions system. The weakness of financial intermediation impedes the progress of structural adjustment, with its focus on the re-dynamization of the private sector.

11. Except in Burkina Faso and Togo, similar crises of varying seriousness have erupted in other countries of the West African Monetary Union (UMOA: Union Monétaire Ouest Africaine) stemming largely from underlying weaknesses of the system. The Bank has been discussing systemic issues with the Central Bank of the zone, and the discussions have led to the reforms outlined below. These aggressive reforms constitute an

adequate framework for the restructuring of the financial sector, not only in Senegal but in the other UMOA countries as well. They also provide a sound basis for the medium-term development of the flexible financial systems and capital markets needed for economic growth.

12. Some first steps toward reform of the banking and financial sector began within the SAL process. Under SAL III, a review of the operations of the banking system was completed which documented the extent of the crisis and provided the elements for putting together an agenda for reform under this operation. Following this review, the minimum capital requirements of the banks were raised, the Banking Association was revived, and the tax on interest earnings was lowered and subsequently eliminated.

A. BACKGROUND

The Banking System

13. Senegal's banking system has 15 banks. The Government of Senegal holds equity in nine banks and has exercised direct control in five of them. In 1986 a liquidity crisis affected eight of the 15 banks, including two larger ones that had accumulated overdrafts of CFAF 50 billion (about US$180 million) with the Central Bank (BCEAO: Banque Centrale des Etats de l'Afrique de l'Ouest). To deal with their liquidity problems the distressed banks had increasingly resorted to borrowing from the BCEAO. However, when this latter stopped, in 1988, providing them with additional refinancing facilities, their operations came virtually to a halt. The following table summarizes the financial situation of the Senegalese banking system as of September 30, 1988.

Table 1: SUMMARY SITUATION OF THE BANKING SYSTEM

(CFAF billion, US$ million)

	Eight distressed banks		Sound banks		Total	
	CFAF	US$	CFAF	US$	CFAF	US$
Loan Portfolio	323	1,023	166	526	489	1,549
Non Performing loans	233	738	6	19	239	751
Capital & Reserves	36	114	29	92	65	206
BCEAO refinancing	167	528	30	95	197	623

14. Problems in the banking sector have arisen from economic and institutional factors common to the countries of the West Africa franc zone. Unfavorable economic conditions -- droughts in the early 1980s, and adverse shifts in the terms of trade -- weakened the banking sector. Institutional problems exacerbated these negative economic effects. The problem banks had been plagued by poor management, government interference, and lack of internal controls on lending decisions. Finally, because of the division of responsibility between the BCEAO and national authorities, inspection and control of banking operations has practically

been nonexistent, so that few sanctions were applied against the misuse or mismanagement of funds.

The Policy Environment

15. The Senegalese banking/financial sector and its problems can only be understood within the context of the rules and regulations of the UMOA, whose membership includes Benin, Burkina Faso, Cote d'Ivoire, Mali, Niger, Senegal and Togo. The Union has four essential provisions for monetary integration. First, a freely convertible common currency -- the CFA franc -- whose exchange rate is supported by an overdraft facility (operations account) of the French treasury has been fixed vis-a-vis the French franc for more than 40 years. Second, there is an interest rate structure which is uniform throughout the zone. Third, uniform ceilings on bank lending margins are fixed with reference to the common interest rate structure. Fourth, common limits on government borrowing from the Central Bank are set at a cumulative total of 20 percent of the previous year's fiscal revenues.

16. With few restrictions on current and capital transfers, the franc zone system is highly open, and under these circumstances the Central Bank has little control over the money supply. To keep the operations account position within acceptable limits, the level of net foreign assets is taken as the principal policy target of Central Bank operations. 1/ The Central Bank controls the level of net foreign assets essentially by controlling rediscounts of private sector borrowing and advances to governments. If credit creation, either through rediscounting or advances to the governments, exceeds domestic requirements as determined by nominal GDP growth, unneeded liquidity flows out of the economy, bringing a deterioration in the balance of payments and a reduction in net foreign assets. If credit is restricted relative to domestic requirements, liquidity flows inward, and the net foreign asset position improves.

17. Thus the Central Bank sets global credit targets (ceilings) that are consistent with forecasts of nominal GDP growth rates for the individual countries. Forecast requirements for domestic credit are then translated into annual targets for Central bank refinancing. Before shares in country rediscount ceilings are assigned to the primary banks, a provision is made for advances to member country treasuries within the limit of 20 percent of the previous year's fiscal revenues. As a prudential measure, Central Bank financing through rediscounts is limited by statute to 35 percent of an individual bank's total credit, although the actual ceiling may be considerably lower.

18. Until 1980 the Central Bank controlled the evolution of bank credit solely through refinancing (rediscounts). In 1980 separate credit (lending) ceilings were introduced bank-by-bank as a further control on overall credit growth. The system is thus somewhat overdetermined, since global and country limits on Central Bank rediscounts should suffice under

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1/ This policy is reinforced by the strong concern of the French Treasury that a negative operating account position does not become a permanent feature of the zone.

the UMOA system. Within the member countries, credit (and rediscount) ceilings for private sector lending are administratively assigned to individual banks by the national credit committees. 2/ While credit ceilings are communicated to the banks and set monthly, banks are not informed of their rediscount ceilings.

19. Once annual global credit ceilings are established, there is no mechanism to adjust them (or reallocate them among member countries) to accommodate variations in a member country's money supply that may be required to meet external shocks. The same applies to rediscount ceilings. This means that it is virtually impossible under the current system to adjust credit to offset unexpected changes in the terms of trade, the deflationary impact of structural adjustment programs, or unexpected reductions in growth rates arising, for example, from droughts. Moreover, with country ceilings fixed under the global credit ceilings, considerable inflexibility is built into the bank credit allocations as well.

20. Until recently Central Bank rediscounts were generally supplied at the "normal" discount rate (TEN: taux d'escompte normal), or for loans targeting priority sectors, at the preferential rate (TEP: taux d'escompte privilégié). Bank margins were fixed zone-wide for different types of lending and applied to these discount rates whether or not loans were financed from deposits or rediscounts. Rediscount rates were adjusted in line with Paris rates. In 1975 a zone-wide money market was established with an administered rate (TMM: taux du marché monétaire) generally maintained in somewhat closer alignment with Paris rates than the TEN, largely to keep banks with excess funds from transferring these resources to the Paris market. 3/ Increasingly the BCEAO has directed bank borrowings to the money market, whose rate has generally been above the TEN. Demand for loanable funds for the zone as a whole -- arbitrated by the BCEAO-intermediated money market (in effect, another form of rediscounting) -- far outstrips supply, and the difference between supply and demand is provided by BCEAO within the framework of country and bank rediscount ceilings. In 1988 the BCEAO provided about 30 percent of its total financing to the monetary union through this facility, while only 3 percent was supplied through ordinary rediscounts at the TEN. Rediscounts of crop marketing credits, not counted under credit ceilings, have historically taken up about two-thirds of total preferential credits.

21. Effects of the system on financial intermediation. The UMOA system has prejudiced the development of financial intermediation. Banks that have reached their particular rediscount ceilings are unable either to borrow from the money market or to have access to interbank borrowings,

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2/ Members of this committee in Senegal include the Ministers of Finance, Plan, Industry, Rural Development and Commerce. Since 1988 the committee also includes the Governor of the BCEAO and a representative of France. Its Secretary is the Director of the National Agency of the BCEAO.

3/ In addition, strictly interbank markets have developed within several UMOA countries. Unlike the money market, these markets are not mediated by the BCEAO. Total amounts traded on these markets have been very limited.

interbank sales of CDs and other types of monetary instruments that involve exchanges of liquidity or term transformation. Similarly, even if banks are within their rediscount ceilings, their credit ceilings may discourage them from trying to mobilize deposits or other sources of liquidity that they will be unable to use to develop their business. Thus the way in which the BCEAO has managed liquidity has stunted the development of member countries' banking and financial intermediation systems to the point where the financial market is almost exclusively limited to bilateral relationships between the primary banks and the Central Bank.

22. The national credit committees' discretionary power to fix bank credit ceilings has given rise to large-scale government interference in the banking system to the benefit of the weakest banks. The problem banks have had preferential access to BCEAO rediscounting as well as to higher credit ceilings, which allowed their balance sheets to deteriorate even more. The figures shown in Table 2 indicate that the credit ceiling system, combined with Central Bank rediscount policy, tends to discourage the growth of sound banks and encourage the growth of the problem banks. The growth of the problem banks was in effect largely financed by deposits from the healthy banks, channeled through the money market and lent through the BCEAO.

Table 2: CREDIT GROWTH AND BCEAO REDISCOUNTS

Credit Growth in Senegalese Banks, 1985-1987
(percentage)

	1985-86	1986-87
Sound banks	3.5	3.9
Problem banks a/	7.8	13.6

Credits and BCEAO Rediscounts Outstanding, September 30, 1987
(CFAF billions)

	Credits	BCEAO Rediscounts
Sound banks	145.6	22.5
Problem banks	316.6	149.2

Source: BCEAO. Resources include those channeled through the money market.
a/ "Problem banks" are those being restructured.

23. Table 3 shows the full dimension of Senegalese banking problem and the extent to which the BCEAO had, directly or indirectly, become a major source of finance for bad loans.

Table 3: CONSOLIDATED BALANCE SHEET FOR THE EIGHT DISTRESSED BANKS, 9/30/88
(in CFAF billions)

ASSETS		LIABILITIES	
Cash and banks	40	Banks	34
Sound credits	90	BCEAO	167
Bad loans	233	Deposits	142
Misc. debtors	36	Misc. creditors	37
Fixed assets	17	Capital/reserves	36
Total	416		416

B. POLICY AND REGULATORY REFORMS

Background

24. BCEAO saw the extensive banking crisis in several member countries in late 1988 as an opportunity not only to restructure the banking sector but also to lay a foundation for developing modern, responsive capital markets. This would involve BCEAO's progressive disengagement from the use of rediscounting to finance private lending activities and allowing the market to develop the financial instruments and institutions to improve the mobilization of private sector resources and their intermediation between savers and ultimate borrowers. Given the fragility of several of the banking systems, it would be unrealistic -- even undesirable -- to introduce purely market-driven financial systems in UMOA now. The first priority is to put financial institutions back on their feet under effective bank surveillance and management, with the cost of restructuring shared by delinquent debtors, the Central Bank, and the Government.

25. In this context -- following consultation with the IMF, the Bank, and bilateral donors (France and the United States) -- the BCEAO took steps toward the needed reforms. As concerns bank restructuring, the UMOA Council of Ministers of June 8, 1989, agreed to consolidate on concessional terms (15 years, including three years' grace, at three percent interest) most of BCEAO's claims on the banks to be restructured or liquidated. On August 1, 1989, the UMOA Council of Ministers approved a complete overhaul of mechanisms for bank supervision and control. This will entail a shift in responsibilities toward the BCEAO itself, the creation of a supranational Banking Commission with jurisdiction in each country, and major revision of the UMOA banking laws to prevent past excesses. BCEAO, the member governments, and the donors view this reform as a keystone for the success of the reform packages.

26. Otherwise, resolution of more immediate problems is emphasized to make the sector more amenable to the introduction in the long run of a more market-based system. The most substantial reforms adopted affect regulations that tended to weaken individual banks' balance sheets. Thus the reforms will sharply restrict the abuse of crop credits and government guarantees on parastatal borrowings which in the past severel jeopardized

bank profits -- even solvency. Reforms in the structure and determination of interest rates -- particularly in providing for widened banking margins -- should also improve bank profitability and stability. Details of the various reforms and their impact on financial performance are examined below.

Interest Rate Policies

27. The BCEAO took some initial steps toward a more market-oriented interest rate policy during the first half of 1989, narrowing the differential between the TEN and the TEP, which had been two and a half percent, to one percent. In its August meeting, the UMOA's Council of Ministers decided to suppress the TEP and TEN altogether, and to use the money-market rate (TMM) as the central rate. 4/ Its level was initially to be aligned with Paris rates and eventually determined by supply and demand.

28. The Council of Ministers also agreed that the BCEAO would (a) channel all rediscounting needs through the money market, which it would continue to intermediate at the administratively determined rate, (b) meet demand for borrowings in excess of money market deposits through a last-resort facility of the Central Bank, whose discount rate (TES: taux d'escompte) would be higher than the TMM, and (c) use the TES as the base to which allowed margins would be added. These measures are to be supplemented by a streamlining of bank commissions and rates.

29. Bank margins. Bank lending margins, which are fixed zone-wide, have -- depending upon the sector -- been applied to the TEP or the TEN whether loans are financed from deposits or rediscounts. It was thus entirely possible for loans to be made at a rate below the marginal cost of funds. It was generally believed in the zone that small-scale or other "privileged" borrowers depend on low interest rates, so margins were often set at levels inversely proportional to the risk associated with the loan being financed. The spread over the TEP was normally limited to one percent for crop credits so marketing agencies began substituting cheap crop credits for working capital credits. Margins on loans to SMEs were fixed at a maximum of three percent over the TEP, not enough to compensate for both risks and overhead associated with loans to these entities. Spreads for all other borrowing were permitted to reach only five percent over the TEN. With the new policies, spreads would be three percent above TES for short-term loans and five percent above TES for long-term loans. Since the marginal cost of funds is likely to be close to the TMM this would effectively widen bank margins. Under current unsettled circumstances -- and given the limited competition among banks in several countries -- in the zone, BCEAO considers it unwise to aim at total liberalization of rates at this time. Should the new measures produce clearly insufficient margins, the Bank will continue to work toward wider spreads.

4/ Advances to governments have hitherto been made at the TEP. These would continue to benefit from a preferential rate one percent below the TMM, set at 10.25 percent in early October 1989.

Credit Allocation Policies

30. Major issues associated with the system of credit allocation administered by the national credit committees include: (a) bank-by-bank credit ceilings, (b) crop marketing credits, (c) sectoral credit targets, (d) the prior authorization mechanism, and (e) government guarantees of state-enterprise borrowings.

31. Bank-by-bank credit ceilings. The administered allocation of credit ceilings has aggravated the collapse of Senegalese banking by allowing weak banks more than their share of allowable credit. In August the UMOA Council of Ministers decided to introduce measures making the bank-by-bank credit ceiling allocations somewhat more flexible until the ceiling system could be substantially more liberalized. Among other things, credit ceilings were to apply on a quarterly basis, rather than a month-by-month as they do now. This response is only partial. More liberalization is required to allow banks to develop their business and compete on an equal footing, to allow development of the interbank market and of financial instruments -- now lacking -- essential to broaden financial intermediation. Existing BCEAO rules, for instance, would allow, in an individual country, the abolition of bank-by-bank credit ceilings simultaneously with the allocation of rediscounting/refinancing ceilings in such a way that varying liquidity needs could be met through the free use of the interbank market. This approach could give rise to unexpected changes in liquidity, so the necessary fine-tuning would be carried out through mandatory asset-based reserves, which would be remunerated. The Government has agreed to a study on measures that would eventually allow the suppression of bank-by-bank credit ceilings. A condition of second tranche would be consultation on the study results and, if warranted, agreement on procedures and timing for introducing measures that permit the suppression of bank-by-bank credit ceilings and their replacement by more market-oriented mechanisms. 5/ The study of the best approach to the design and implementation of such a system would be undertaken by the World Bank, the BCEAO and the Government, with input from the IMF.

32. In the longer run, when financial markets in the zone have been restructured, liquidity now supplied through rediscounts to individual banks on an administered basis could be provided zone-wide by the Central Bank through a periodic (say, weekly) auction of rediscounts on a purely market basis. This could also be an interest-rate setting mechanism. To the extent that local circumstances -- from droughts or sharp changes in the terms of trade -- justified it, differential reserve requirements could

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5/ A certain degree of arbitrariness would still be required in a system that could not be fully market oriented (because of Senegal's membership in the zone). Country-level rediscount ceilings could be maintained as now, but their allocation among banks could be made on the basis of simply and openly administered criteria. Thus a bank's rediscounts from the Central Bank could be determined on the basis of its sound credits, as a percentage of the total amount.

be set among individual member countries, either offsetting negative external effects or sterilizing (to the extent required) unexpected positive flows.

33. Crop Marketing Credits. Crop marketing credits are short-term advances that finance the full collection cost for agricultural products from producer through final sale. They have disrupted the financial system in Senegal and other member countries . Since reimbursement is generally expected within the year, they have not been subject to credit ceilings. To encourage production, the Government has often set producer prices (including collection, processing and marketing costs) higher than export prices but has been unable to pay the subsidy to the banks participating in the crop credits. Under Central Bank regulations, the unreimbursed portion has to be carried over as a normal credit to the crop marketing agency, guaranteed by the Government and counted against the country's credit ceiling. Serviced only sporadically, these unreimbursed crop credits have tended to accumulate becoming a major burden on the banking system, absorbing a good part of annual increases in credit ceilings, and crowding out the productive sector.

34. ONCAD, Senegal's defunct groundnut marketing and processing agency, is a case in point. Its dissolution in 1982 left the BNDS, a public bank, holding unreimbursed claims totaling CFAF 94 billion, CFAF 64 of which was the unrepaid capital sum, and CFAF 30 billion unpaid interest. The major local banks were obliged to take up shares of the outstanding balance, and the BCEAO agreed to rediscount CFAF 64 billion. Debt service payments due from the Government as ONCAD's guarantor are roughly CFAF 13.5 billion a year, but are being paid only irregularly. Thus ONCAD's refinancing not only crowded out other borrowers in 1982 but has remained a source of balance sheet problems for the banks involved.

35. Because the crop credit problem affects virtually all countries in the zone, it was given close scrutiny by the BCEAO and was the object of far-reaching decisions at the August UMOA Council of Ministers meeting. Those decisions aimed at bringing total bank financing of crop credit in line with expected export receipts, providing an overall financing plan and identifying ex ante sources of finance for the crop credit in the event that the producer price exceeds the world parity price. In addition, crop credits will henceforth be subject to credit ceilings. This, together with the agreed abolition of the TEP, should reduce the incentive for marketing/export organizations to substitute crop credits for normal working capital financing.

36. Beyond the measures adopted by UMOA, the Senegalese Government has agreed that banks would be permitted to decide for themselves whether or not to take up the proposed credits. This means that banks will not take up the credits unless repayment is assured, which is a strong incentive for the Government to make sure that the financing package is sound.

37. In view of the complexities of the problem and uncertainties about how well the system will function, a condition for second-tranche release will be a review of the new system's operations -- in consultation with the

BCEAO and the Bankers' Association (APB) -- and implementation of any needed corrective measures to improve its functioning.

38. Sectoral Allocation of Credit. The system of targeted credit established objectives for the proportion of bank credit going to sectors designated as "priority" (such as lending to SMEs, or for social housing). Target levels were set and administered by the National Credit Committees. Even under the best of circumstances, however, it was difficult to guarantee the end use of targeted resources, given the fungibility of money, so even if nominal quotas were met, financial resources may not have flowed to the intended beneficiaries. Seen from another perspective, the targeted credit policy provides the Government with considerable direct leverage over lending decisions. In public banks, for example, total loans to priority sectors far exceeded sectoral lending guidelines. In other commercial banks, sectoral targets have been applied sporadically -- to coerce banks into taking up crop credits, for example -- but have not had much effect, even nominally.

39. Outright abolition of these guidelines would not disrupt the financial system. The Council of Ministers of August 1989 abolished the guidelines for targeted lending.

40. Prior authorization mechanism. The prior authorization mechanism is applied when a loan would put a customer's total borrowing from the banking system above a set level, which is fixed at CFAF 70 million in Senegal. 6/ The BCEAO justified the procedure as an instrument of qualitative credit control -- to ensure that credit goes to "sound" enterprises and to ensure compliance with sectoral credit targets. 7/ As a practical matter, the procedure has done little to enforce compliance with the sectoral guidelines or to ensure that banks lend only to creditworthy borrowers.

41. Apart from its apparent inefficacy, the procedure is administratively cumbersome: even for completed applications it can take up to two months. This reduces the banking system's ability to respond promptly to the economy's credit needs -- for trade credit, for example. Also, decision-makers can easily misuse bureaucratic discretion.

42. BCEAO has effectively dropped the sectoral guidelines, but is still concerned about borrowers' creditworthiness. Ordinarily, the primary banks evaluate risk themselves and the Central Bank inspects the quality of their portfolio. The BCEAO argues that it is necessary to retain some of the prior authorization mechanism as a safety net to supplement its new banking supervision apparatus. The UMOA Council of Ministers endorsed both a substantial increase in the threshold and relaxations of current procedu-

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6/ With a view to subjecting about 80 percent of all lending to the procedure, it is set at CFAF 100 million in Cote d'Ivoire and CFAF 30 million in the other countries of the zone.

7/ Thus the credit application may be rejected if the lender is out of line with mandated quotas.

res. A second-tranche disbursement will be based upon (a) a review by the Bank of how well the new system functions in Senegal, particularly in terms of efficacy and speed, and (b) the satisfactory implementation of any further reform measures needed. The review would be jointly undertaken with the BCEAO and the APB.

43. Government guarantees of public enterprise borrowing. The past readiness of the UMOA governments to guarantee the borrowings of uneconomic public enterprises has greatly undermined the system. Of the CFAF 144 billion of bad debts held by failing banks in Senegal, more than 20 percent were loans guaranteed by the Government. These loans represent a way for the Government to circumvent the 20 percent rule limiting its borrowings from the Central Bank to the extent that they are made to enterprises accumulating receivables from the Government for goods and services to the public sector. These loans were considered risk-free because of the government guarantee, but were often made to uncreditworthy enterprises. They had a destabilizing impact on bank balance sheets once the Government failed to honor its guarantees. The UMOA Council of Ministers agreed in its August meeting to a number of zone-wide measures that would eliminate most of the commercial banks' incentives to favor government-guaranteed debt: in effect, its treatment under BCEAO procedures would be no more favorable than that for nonguaranteed debt. In addition, guarantees not honored would be counted against the governments' net borrowing positions. Moreover, the Senegalese Government decided on August 12, 1989 to abstain altogether from issuing guarantees for internal borrowing, public or private.

Taxe sur la Prestation de Services (TPS).

44. This tax -- which has been applied to both interest earnings paid on deposits (lowered under SAL III from 17 percent to 7 percent and subsequently to zero) and to interest paid on loans (17 percent) -- hinders financial deepening by substantially increasing intermediation costs to the ultimate borrower and potential profits to the banking sector. A "wedge" between the real cost of capital and the cost to borrowers, it tends to reduce investment. Though the tax on deposits was recently eliminated the tax on borrowing remains and continues to have a distortionary effect.

45. Because of its impact on financial intermediation the TPS on lending should be phased out entirely. Under Senegal's current severe budget constraint, it may be difficult for the Government to forgo the approximately CFAF 2 billion in lost revenues associated with this reduction. Accordingly, a schedule of phased reductions will be agreed upon with the Government in June 1990, with the goal of complete removal within five years.

Bank Supervision

46. Responsibility for bank supervision and inspection was split between the BCEAO in charge of actual inspection and the national authorities (the Ministry of Finance and the Banking Control Commission) in charge of determining and applying any sanctions resulting from the inspections. The system has failed on both accounts. Until recently inspections were rare

and recommendations (which were not discussed with the primary banks) were rarely followed because Governments had no incentive to correct a situation they had often helped create. Flaws in the system of external control were compounded by the absence of internal controls of the banks not having close ties with foreign banks. Control systems were ignored at all levels: by internal auditors, management, and the Boards of Directors.

47. In its discussions with the donors, BCEAO readily agreed that control systems had to be brought into line with normal industry practice. The major issue was how -- assuming that BCEAO headquarters staff would carry out regular, satisfactory inspections -- one could make sure that the recommendations would be enforced. The BCEAO had no jurisdiction in these matters in the member countries. Proposed solutions ranged from a national Banking Control Commission -- strengthened by the membership of the Governor of the Central Bank and a representative of France -- to the creation of a supranational Banking Commission. This institution would review the reports prepared by BCEAO inspection staff, would decide on sanctions, and would have the means to enforce its decision in each country. Because the first alternative would lead to the same unworkable division of responsibilities as in the past, the BCEAO and cofinanciers -- particularly France as guarantor of the CFA franc -- argued for the supranational Banking Commission.

48. At its August meeting the UMOA Council of Ministers agreed to two bold measures. First, a zone-wide Commission would be established by October 1990 and include two members from each UMOA country and from France. Second, banking laws and regulations would be revised to prevent the recurrence of past excesses and to bring them in line with practice in other countries. New banking legislation would be effective in the UMOA countries by October 1990. Meanwhile the BCEAO has obtained support from France and the IMF to strengthen its inspection department so it can hold inspections once a year. Work has also begun on the introduction of a uniform bank accounting system.

Impact of the Reforms

49. These reforms should improve financial intermediation over the long term and provide a sound basis for the bank restructuring that is to take place. Further measures must be taken, however, to encourage the development of new financial instruments adapted to savers' and investors' requirements in terms of risk perception, liquidity, and maturity -- and the growth of institutions capable of intermediating between borrowers and lenders so as to optimize supply and demand for financial resources. To some extent these measures must wait until bank restructuring has taken place and the new mechanisms for bank supervision have been shown to work successfully. BCEAO and its partners -- the IMF, the World Bank, France, and the United States -- will continue to work together on further needed reforms.

C. BANK RESTRUCTURING

50. In June 1989, after consulting with the Bank and bilateral donors, the Government of Senegal finalized a comprehensive approach to restructur-

ing the banking system. This approach had three aims. First, it would maintain only banks that, after restructuring, could become profitable, solvent, and liquid. Second, it would reduce government interference in the banks' management through privatization and by limiting the Government's share capital in any bank to a maximum of 25 percent. Third, it would develop a global financing plan with projected annual Government contributions compatible with the Government budget. All restructuring measures are based on independent audits of the banks' accounts, operations and portfolios, as well as all BCEAO inspection reports, when available.

51. To achieve the first objective, the balance sheets of the distressed banks would be restructured so that their net worth would become positive and would meet minimum capital adequacy requirements. In addition, staffing would be reduced, costly branch networks pruned and changes in management introduced. These drastic restructuring measures would ensure that restructured banks can withstand the rigor of competition without being tempted to increase their lending beyond reasonable limits in the hope of making high enough profits to provision bad debts.

52. As a corollary to these principles, unrecoverable assets would be removed from the balance sheets of all the banks to be restructured. Depending on shareholders' willingness or ability to restore financial viability, two different approaches would be used to restructure the eight failing banks:

(a) When shareholders agree to rehabilitate the banks under their control, the restructuring would include -- along with measures to strengthen management and reduce costs -- restoration of the banks' financial situation through shareholder equity or quasi-equity contributions to offset all losses and recapitalize the banks to a level compatible with sound banking standards. 8/ Three banks whose foreign majority shareholders want to stay in business through restructuring would in association with private Senegalese investors follow this procedure: BIAOS (65 percent of which is owned by the French BIAO Group), BSK (partly owned by Kuwaiti interests), and MASSRAF (partly owned by Saudi Arabian interests).

(b) When the financial requirements for rehabilitating a bank are beyond the resources of its shareholders (the case with the government-owned or controlled banks), the balance sheet would be split into a "sound balance sheet" and a "liquidating structure." The sound balance sheet would include the performing loans and an equivalent amount of liabilities (primarily private deposits) and the equity required for a viable bank. The balance sheet of the liquidating structure would consist of the nonperforming assets and bank losses and an equal amount of liabilities, primarily to the BCEAO and, if necessary, liabilities to public and private depositors. This procedure would apply to five government-controlled banks.

8/ Under Senegalese commercial law, bank shareholders are liable only for their equity, unless fraud is involved.

53. Implementation of the restructuring program started in late 1988 and is expected to be completed by the end of 1989. For the three banks of the first group, restructuring plans were drawn up after an independent audit of their accounts, operations, and portfolios. The first phase of BIAO's restructuring has already been implemented. Discussions are currently under way between the shareholders of BSK and MASSRAF and the monetary authorities with respect to the restructuring of these two banks. Completion of restructuring in accordance with their plans, or failing that, the liquidation of these two banks, would be a condition of second-tranche release.

54. For banks of the second group, a protocol was signed in May 1989 by the two shareholders of USB (the Government of Senegal and Credit Lyonnais of France) which split the bank into a financially viable bank which started operation in July 1989, and a liquidating structure. The new institution, Credit Lyonnais-Senegal, with about a fourth of its staff, a fifth of its branches, and a third of its assets, has been recapitalized by Credit Lyonnais (95 percent) and the Government of Senegal (5 percent).

55. On August 1, 1989, the Government put the four other banks into receivership. It proposes to create a new bank to take over the sound assets (and an equivalent amount of deposits) of the four banks. The nonperforming assets would be transferred, along with liabilities, to a liquidating structure. This structure would be merged, with that of USB to become a recovery company in charge of recovering the bad loans that it has inherited. The new bank and the recovery company would start operations on January 1, 1990. The banking licenses of three banks were suspended as of November 1, 1989; the decree for the suspension of the license of the forth by December 31, 1989 was issued on November 15, 1989. The four banks would be liquidated beginning January 1, 1990.

56. The new bank would be a small one with assets of about CFAF 22 billion (about US$70 million) remaining from the CFAF 180 billion (about US$600 million) in assets of the liquidated banks. It is expected to be a commercial bank whose capital would be subscribed in majority by private individuals, local insurance companies, and a commercial bank that would assume its management. Government shareholding would be a maximum of 25 percent. It has been agreed that until a managing partner has been found, the bank's activities would be limited to (a) managing its existing portfolio; (b) receiving small deposits, which the commercial banks are increasingly refusing; and (c) lending only to existing creditworthy clients and placing liquid funds on the money market. 9/ Until a commercial partner is found the bank will receive technical assistance financed by USAID.

57. The privatization program. In a number of circumstances the Government has used its ownership position to influence bank lending decisions in ways that have been detrimental to sound banking. This has been

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9/ Financial projections show it would be viable even with limited operations.

an important source of banking problems in Senegal. The Government has decided to take steps to prevent the recurrence of such practices by reducing its share capital in any bank to a maximum of 25 percent, which is less than is required to be a blocking minority. The Government's share capital in the restructured BIAOS and Credit Lyonnais-Senegal has already been reduced to 25 percent and 5 percent, respectively. To complete its divestiture program, the Government envisages (a) further reducing its ownership in BIAOS to about 18 percent by not participating in the next capital contribution provided for in the restructuring plan; (b) selling shares in the other banks in which it holds, directly and indirectly, more than 25 percent (namely CNCAS 10/ and BICIS) before the end of June 1990; and (c) limiting its participation in the new bank resulting from the liquidation of the Government banks to a maximum of 25 percent. Reduction of Government's direct and indirect participation in CNCAS and BICIS would be a condition of second tranche release.

58. The promotion of grass-roots institutions. After the liquidation of Government banks and the privatization of the others, the restructured banking system (except for the new bank) will consist of commercial banks catering mainly to large depositors and trade financing. There is a risk that a layer of the population -- small depositors, small scale enterprises, and farmers -- will find access to banking services difficult. 11/ Therefore the Government intends to encourage, through an appropriate legal and regulatory environment, the development of grass-roots structures whose capital would be held by depositors, and which would operate on a cooperative or mutualist basis.

59. This type of financial institution would be an efficient channel for mobilizing savings and providing credit to rural and urban customers excluded by commercial banks. It is expected that credit risk would be reduced as peers of the borrowers would assess credit applications and provide for social sanctions in case of default. Some promising initiatives -- promoted by bilateral donors and various nongovernment organizations -- are presently under way in Senegal. In the rural sector USAID and CNCAS are promoting small savings collection/mutual credit schemes. Canadian experts financed by CIDA are setting up a similar scheme for a community of fishermen in Dakar. Another Canadian technical assistance project is converting the postal savings and checking network into a grass-roots structure that would be linked to the financial system rather than to the Treasury, as it presently is. To promote the rapid development of a nationwide network of such institutions -- such as the "Union des Banques Populaires" which has efficiently mobilized savings in Rwanda -- the Ministry of Finance intends to (a) gather information on these experiments to understand the causes of their success or failure; (b) support the creation of mutualist institutions in the urban areas not covered by these initiatives; (c) work out, with the organizations involved, an action plan

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10/ The Government shares in CNCAS would be sold to in priority to the Senegalese federation of nongovernment organizations.

11/ The restructured BIAOS has already rejected deposits lower than CFAF200,000, or about US$700.

for the timely confederation of these institutions under a national institution that would manage their liquidity, provide specialized technical assistance, and provide credit to customers neglected by the banks; (d) put in place arrangements for proper supervision of these institutions; and (e) propose changes in the legal and administrative framework that would be needed to make all this happen.

60. CIDA has agreed to finance a Canadian technical assistance team that is expected to be in the field by early 1990 to help the Ministry of Finance carry out the tasks outlined above. These experts' terms of reference have been agreed upon; agreement on the action plan would be a condition of second-tranche release.

61. Bad debt recoveries. An IDA-financed consultant review has shown that the legal provisions for bad debt recovery are broadly adequate to the task. The problem appears to be the complexity of procedures involved, which are similar to those prevailing in developed countries. Convinced that bad debt recovery is critical to fair burden-sharing, the viability of the bank restructuring financing plan, and establishment of the social discipline that would help prevent a buildup in arrears from recurring, the Government has indicated that it would make all arrangements necessary to intensify and accelerate recovery of arrears.

62. Accordingly, the Senegalese Government has proposed to establish a fully government-owned recovery company, staffed partly by personnel laid off by the restructured banks. It would be granted the right to seize debtors' financial and material assets without having to go to court. Its task would be to recover the bad loans of the restructured banks through direct cash repayments or seizure of debtors' assets, loan rescheduling, and other arrangements. This proposal has been discussed in detail with the Bank. Since potential private shareholders approached by the Government have declined to participate in the recovery company, the Government is exploring ways to ensure its efficient operation -- for instance, by linking salaries to amounts recovered and by subcontracting part of the work to specialized private institutions. The Government and IDA have reviewed and agreed on the statutes and arrangements for the recovery company. USAID has agreed to finance the required technical assistance.

63. To facilitate the recovery of bad debt and to ensure that progress is adequately monitored, an independent auditor has prepared a data bank including all information relating to individual delinquent debtors of the banks being restructured. The data bank would be continuously updated. Progress on recovery would be followed by a Blue Ribbon Committee established by the Minister of Finance. This Committee would provide quarterly reports on progress in loan recoveries to the Minister of Finance as well as to the donors. It would also recommend any necessary corrective actions and supervise their implementation.

64. Government estimates indicate that approximately CFAF 32 billion (about US$100 million) of the CFAF 144 billion (about US$450 million) of nonperforming credits of the banks to be restructured can ultimately be recovered over the next four years. The Bank and the Government have

agreed on quantified targets that should be reached semiannually while the program is being implemented. Recovery of the amount targeted for June 30, 1990 (CFAF 9.8 billion), would be a condition for the release of the second tranche on or before this date. Release of the second tranche at any time after this date would require the recovery of the amount which has been targeted for that date in the financial workout.

65. Cost of the bank restructuring and financing plan. The liabilities that the Government will have to assume as a result of restructuring amounts to about CFAF 182 billion (or about US$600 million). This comprises a debt to the BCEAO and other banks (CFAF 131 billion) and to depositors (CFAF 50.7 billion). In addition to these liabilities, the Government would have to make a CFAF 14 billion cash contribution to compensate the restructured banks that have taken over more deposit liabilities than performing assets and to assume the cost of layoffs associated with the restructuring. The total cost of the bank restructuring will therefore amount to about CFAF 196 billion. The BCEAO has agreed to convert bank debts of CFAF 126.5 billion into a term loan payable over 15 years, including three years' grace at three percent a year. On the due dates, the resulting installments would be automatically debited from the Government's accounts in BCEAO's books. The debt to depositors, the other banks, and the cash contributions to the banks mentioned earlier will be paid by the Senegalese Government through the expected CFAF 32 billion of proceeds from bad loan recoveries with a budget contribution of CFAF 37.5 billion, to be financed partly with external budget support. The resulting cash outlay from the budget is estimated at CFAF 10 to 15 billion yearly over the next 15 years, an amount that should be compatible with Senegal's budget. Government fulfillment of its obligations under the financing plan will be a condition of second-tranche release.

D. SOCIAL IMPACT

66. The impact of bank restructuring on sector employment is high, and some 700 jobs of a total of 1700 are expected to be lost. But safety nets are available to mitigate the impact on those losing their jobs. The banks in question will expend a total of CFAF 3.2 billion in severance and retraining pay, which works out to an average of 32 months' salary for the individuals involved. A retraining program, similar to the one successfully implemented by BIAOS, would help retrenched employees create their own business, possibly with the support of the National Employment Fund (created under SAL III).

67. Another social cost associated with the FSECAL is the increasing inaccessibility of the commercial banking sector to small borrowers and depositors. For this reason the operation seeks to establish the bases for a grass-roots banking system based on mutualist principles. The establishment of such institutions will take some time, but it is expected that the new bank resulting from the merger of government-controlled banks and the revitalized postal savings and checking systems will respond to the needs of depositors in the interim.

PART III - THE PROPOSED PROGRAM

A. Program Objectives

68. The major objective of the proposed financial sector adjustment credit is to restore and develop a well-functioning, broadly based financial sector the health of which is critical to continued progress in Senegal's structural adjustment efforts. It would support an action program set out in the Letter of Sectoral Development Policy the main goals of which would be (a) to introduce institutional and systemic changes that should ensure against systemwide failure; (b) to restructure Senegal's insolvent banking sector; and (c) to set the stage for further improvements in the financial intermediation system.

B. Amount of Cofinancing and Credit

69. Substantial cofinancing by France (US$34 million) and the United States (US$33 million) is in place. Together with IDA-financing of US$45 million, total external resources to be provided will be about US$112 million. In effect, however, in financing CFAF 126.5 billion (or US$390 million) on concessional terms, the BCEAO is the major cofinancier of the operation. The borrower would be the Government of Senegal.

C. Tranching, Procurement, and Disbursement

70. Tranching. The proposed credit would be disbursed in two tranches, the first becoming available on effectiveness, the second nine months after disbursement of the first. In view of extensive reforms already undertaken, 60 percent of the credit would be disbursed in the first tranche. Disbursement of the second tranche would depend upon a review of progress made in implementation of the program as well as satisfactory implementation of the conditions mentioned in para. 71, as these may be required.

71. Procurement. Procurement procedures have been designed to permit rapid use of the funds while ensuring efficiency and accountability in the process. Contracts exceeding US$2 million equivalent would be subject to international competitive bidding. For contracts below US$2 million, public agencies would follow standard practices which have been found to be acceptable in the past. The private sector would follow established commercial practices, and, wherever possible, quotations from eligible suppliers from at least two countries would be sought. Direct contracting would be used only for proprietary items or where compatibility with existing equipment would call for standardization. Procurement documentation would be maintained for ex-post review by IDA. Verification of imports will be limited to inspection for quality and quantity by the Customs Department, which is to be strengthened under a plan of action to be supported by SAL IV.

72. Disbursement. The proceeds of the credit would be used to reimburse 100 percent of the CIF cost of eligible general imports. Public and private sector imports would be eligible, except for:

(a) negative list;

(b) imports of goods procured under contracts costing less than US$ 5,000 equivalent;

(c) imported goods already financed under tied bilateral or multilateral credits; and

(d) imported goods purchased in the local market.

73. The Government would establish a Special Account at the Central Bank in an amount equivalent to US$3 million to facilitate disbursements. The account would be replenished regularly on the basis of fully documented disbursement applications in excess of US$1 million or on the basis of statements of expenditures for expenditures below that amount. The Central Bank would maintain all relevant supporting documentation for review by IDA supervision missions. Retroactive financing would be permitted for an amount not exceeding 20 percent of the total credit amount for eligible imports procured no earlier than four months prior to credit signing. It is proposed that not more than US$10 million equivalent each would be allowed for imports of petroleum and food.

D. Management, Monitoring, and Reporting of the Program

74. Senegal's structural adjustment programs have been effectively managed by an interministerial committee since SAL II. Given the purely financial nature of the proposed program, however, the main interlocutor would continue to be the Ministry of Finance, with whom major questions bearing upon bank restructuring, banking supervision reform, the design of a recovery program for bad debts, and macropolicy issues must be discussed and agreed upon. Quarterly reports on bad debt recoveries (para. 63) and bank inspection reports would come to us through the Ministry of Finance. Much of the work associated with implementation of the program would have to be carried out with the BCEAO, with whom we expect to maintain the good working relations that were established during the preparation of this operation. We will also continue to collaborate with the IMF, France and the United States, particularly for further work that will be required for second tranche release. Moreover, we expect to call upon the Professional Bankers' Association (APB) to help review progress on crop credit and reform of the prior authorization procedure.

75. The Letter of Sectoral Development Policy. The letter, which forms the basis for the FSECAL, and in which the Government declares its commitment to the proposed program, has been finalized during negotiations and officially received by the Bank.

76. Condition of Second Tranche Release

(a) Consultation on the results of the study of measures permitting the suppression of bank-by-bank credit ceilings and, if warranted, agreement of procedures and appropriate timing for the replacement of these ceilings by more market-oriented mechanisms (para. 31);

(b) Satisfactory review of the functioning of new systems of crop credits and prior authorizations by the borrower, BCEAO and APB. Where reviews showed deficiencies, corrective measures would have been taken to improve functioning of the prior authorization system or of the new crop credit system (paras. 37 and 42);

(c) The financial restructuring of BSK, MASSRAF and BIAOS would have been completed (para. 53);

(d) The Government would have reduced its direct and in direct shareholding in each bank and financial institution to less than 25 percent (para. 57)

(e) Agreement on a program of action to facilitate the establishment of a network of grass-roots banks (para. 60);

(f) An acceptable bad debt recovery level would be reached (para. 64);

(g) The Government would be current in the payment of all its liabilities incurred in the financial restructuring package (para. 65); and

(h) Performance in the implementation of the Government's ongoing macroeconomic adjustment program would be satisfactory.

E. Coordination with the IMF

77. Coordination with the IMF on the FSECAL was critical during preparation, particularly inasmuch as the proposed FSECAL has been associated with a number of major policy reforms at the UMOA level which were worked out jointly with the IMF. Coordination with the IMF will continue to be intense with respect to the details of reform measures yet to be worked out as well as their operational consequences. Our collaboration on this issue with the Fund has been good in the past, and we expect it to continue.

F. Benefits and Risks

78. Benefits. The potential benefits of this FSECAL are substantial. Not only should it result in a rehabilitation of the Senegalese banking system -- as well as in reforms that should preclude a repeated crisis -- but it should also establish an improved financial intermediation system that should ultimately aid in the mobilization and term-transformation of financial resources and in their channeling to borrowers hitherto largely excluded from access to credit. The project is thus a necessary complement to measures aimed at private sector development provided for under SAL IV: without an effectively performing banking sector it is unlikely that Senegal will be able to break out of the doldrums that currently affect its economy, particularly the industrial sector.

79. Risks. The potential risks associated with this sector adjustment credit should be acceptable, given the fact that many reform measures associated with the operation have already been undertaken. However, there is a potential financial risk in that a slow recovery of bad debts may jeopardize Senegal's budgetary equilibrium and eventually force payment delays to depositors. Apart from the equity considerations involved, this may in itself have undesirable repercussions both on financial liquidity as a whole and on public attitudes toward the banks.

PART IV - BANK GROUP STRATEGY AND OPERATIONS

A. Country Assistance Strategy

80. Bank strategy in Senegal has two broad and interrelated objectives. The first objective is to assist the Government in the short/medium term in rectifying structural imbalances in the economy which are the cumulative result of internal and external shocks as well as policy distortions over several years. The means employed have been to improve the incentive environment and to promote greater efficiency in economic management. The instruments to support this objective have been adjustment lending, buttressed by appropriate technical assistance operations. The second objective is to promote a sustainable level of long-term growth and development. The instruments designed to address this objective are sector-based rehabilitation/investment projects, within an appropriate framework of sectoral policy reforms.

81. The country's development strategy, as spelled out in the most recent Policy Framework Paper for 1989/90 to 1991/92, lays heavy emphasis in the short term on improving incentives for private investment; rehabilitating the banking system and deregulating the financial sector; and improving resource utilization and expenditure control in the public sector. These objectives are supported by the policy reforms to be supported through SAL IV which is being processed in parallel with this operation. Together, these two operations are expected to improve the utilization of existing production capacity and thus improve the competitiveness of Senegalese industry. Furthermore, they would increase the volume and improve the quality of investments both public and private and thus enhance growth prospects in the medium term. Beyond 1992, Government recognizes the need to rebuild productive capacity even as the stabilization and structural reforms begun earlier continue. Thus, the public investment program for that period includes major projects in energy distribution and in water supply and highway rehabilitation and maintenance, for which IDA financial assistance has been requested. The proposed lending program in the period beyond FY91 is thus balanced between investment programs in urban infrastructure and services (sanitation, water, energy) and policy-cum-investment operations which focus on further private sector development, on environment and on human resources development.

82. Given Senegal's membership of UMOA and of the CFA Franc Zone, the depreciation of the real exchange rate which is required to increase the external competitiveness of the Senegal economy would be achieved by

implementing, over an extended period of time, appropriate demand management policies together with additional measures to reduce production costs and to encourage production of tradables. Nonetheless, Senegal is expected to be able to meet its objectives over the medium term, provided it consistently applies that required policy measures which are being supported through this operation and through SAL IV.

A. Bank Group Operations, Past and Future

83. As of September 30, 1989, the Bank Group had approved 88 operations in Senegal for a total of about US$916 million, consisting of 57 IDA credits (including three Special Fund credits), 20 Bank loans, together with two SFA, and nine IFC operations. To date, 39 credits and the 20 loans have been fully disbursed. Of the 24 active projects, 5 are in agriculture or rural development, 4 are in industry and energy, 6 in infrastructure, 3 in human resources; there are also 6 TA and adjustment operations. The Small Rural Operations II Project ($16 million) was approved in March 1989. As discussed above, for the next few years Bank assistance will focus heavily on adjustment, particularly at the sectoral level.

84. In the area of Structural Adjustment, the SAL II and SAL III operations have been successfully completed. 12/ The main reforms initiated under SAL II consisted of improvements in the industrial incentives system; liberalization of agricultural input supply and rice marketing; and improvement in the management of public resources. Most of the reforms supported under SAL III represented a continuation and a deepening of those initiated under the preceding SAL. Additional actions included initial measures to improve financial intermediation, the formulation of population policy, and the alleviation of the adverse transitional impact on employment caused by structural adjustment.

85. After SALs II and III, Senegal's economy has been substantially liberalized, with free movement of goods within the country largely unencumbered by price controls, and imports unhindered by quantitative restrictions. The private sector now plays a more important role, especially in trade and the processing of agricultural products. Progress has been made in fiscal and debt management. Investment programming has been strengthened and the system of economic planning is being reformed. A population policy was adopted and an action program is being implemented. In contrast, progress was less than anticipated in three other principal areas. Whilst most planned financial sector actions were implemented, the dimension of the banking system crisis was underestimated by both the Bank and the Government (para. 12). Labor hiring practices were reformed though Government was unable to pass legislation that would have increased labor market flexibility in a meaningful way. The public enterprise sector continues to be a major financial burden on the economy despite the implementation of a program of reforms. In particular, though progress was made in identifying public enterprises for privatization, it is only

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12/ A Program Completion Report for SALs II and III (June 1989) is available.

recently that the program of public enterprise privatization began to have some response. As a result, the Senegal economy is now more open and exposed to competition from abroad, but significant constraints remain to be effectively tackled in order for a supply side response to be forthcoming. A major reason for the lagging investment and supply side response is the persistence, despite the measures taken under SALs II and III, of certain rigidities in the economy, and in particular the weight of public consumption (the high wage bill of the civil service and the deficits of the public enterprises), the over-regulation of the labor market and the crisis in the banking sector.

86. SAL IV would thus focus on relatively fewer areas than previous SALs and would support a limited number of critical actions. The key policy areas which will be addressed represent a consolidation and a deepening of policies initiated under the previous SALs, and include: (i) private sector incentives, i.e., reduction in the costs of production (especially labor, energy and transport) and further improvement in the incentives system as well as the regulatory environment; (ii) public sector resource management, i.e., cutbacks in both current spending for the civil service wage bill and transfers to parastatals, better investment programming, and improvement in the revenue base; and (iii) minimization of the social costs of adjustment. Existing technical assistance projects are supporting the formulation and implementation of the various action programs included in the SAL operations, with measures to improve the management of public investment, public debt, personnel information and career development, as well as management of economic information and the development of a policy formulation capacity.

87. The next phase of reforms in the agricultural sector will be supported by the Bank under a separate Agricultural Sector Adjustment Credit (SECAL). This phase will be characterized by policy development in areas complementary to the thrust of the improvements made to date. The overall aim of the SECAL is to support more efficiency and price responsiveness in agriculture, a decrease in government controls, and the elimination of subsidies. In particular, the reforms to be pursued will be: (i) in the cereals subsector, further review of the system of protection with the overall goal of encouraging the production and transformation of coarse grains in which Senegal has a comparative advantage (i.e., millet and sorghum), diversifying production into other crops such as maize, and further liberalizing the rice market; (ii) in the groundnut subsector, action to reduce losses in processing, privatization of confectionery groundnuts and revised protection against imported oils as a precursor to the eventual elimination of all subsidies; (iii) a full review of the agricultural credit system; and (iv) the development of an appropriate land tenure and land management regimes to encourage resource conservation and long-term private investment, especially in the Fleuve region. Measures to reduce losses in the cotton subsector and to promote diversification for exports would also be pursued.

88. The two other sectors where important reforms are to be pursued are transport and human resources. Major improvement is being sought in the planning, operations and management of the transport sector in Senegal. A dialogue has been established with the government since a policy review

meeting with the Bank in 1986. Broad agreement, as included in the Declaration of Transport Policy, has been reached on the need for reforms in three main areas: (i) improved investment planning in the sector with a target of at least 80 percent of investment in the sector earmarked for infrastructure maintenance and rehabilitation, and a stronger emphasis on repairing the dilapidated highway network through 1991; (ii) increased mobilization of resources from the sector through improved efficiency, cost control and revised tariff policies, policies which are expected to be especially vital in the railways and ports subsectors; and (iii) strengthened sector management through a series of institutional reforms, including revising the legal status and increasing the autonomy of the railways parastatal. Improved transport efficiency is a key factor in the process of increasing market responsiveness in the economy and reducing costs of production for agriculture and industry. The envisaged government investment program for the period 1989-93 provides for an increasing role for the private sector, with a minimum of one-third of future road maintenance to be contracted out.

89. The development of the human resource potential of Senegal is of high priority if the growth possibilities created by structural adjustment are to be exploited. The government in consultation with the Bank has identified a number of areas where policy reforms are required: (i) with regard to population policy, legal and regulatory changes are envisaged to counter biases in favor of large families and against women, and a revised priority investment and action program is to be prepared; (ii) with regard to health, total expenditure is expected to grow in real terms to, *inter alia* improve the "field effectiveness" of health services and to implement an essential drug distribution program; and (iii) with regard to education, spending will be refocused on basic and primary education with a target increase in enrollment ratios from the present 56 percent to 65 percent by 1995, and on increasing the autonomy of technical and professional schools to cater for demands other than that of the government services. The Bank expects to support this program through a Human Resource Development SECAL.

PART V - RECOMMENDATION

90. I am satisfied that the proposed IDA Credit would comply with the Articles of Agreement of the Association and recommend that the Executive Directors approve the proposed Credit.

Barber B. Conable
President

Attachments
Washington, D. C.
November , 1989

SENEGAL - KEY ECONOMIC INDICATORS 1_/ 11/13/89

	Actual								Projected									
	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997
Real GDP growth rate	-3.3	-0.8	15.2	2.6	-4.6	3.8	4.5	4.0	5.1	-1.3	4.8	3.9	3.8	3.8	3.6	3.6	3.6	3.6
Real GNP growth rate	-3.5	-1.7	14.9	2.2	-5.3	3.9	3.9	5.2	5.2	-1.4	5.4	4.4	4.2	4.3	4.0	4.0	4.0	3.9
Real GNP per capita growth rate	-6.2	-4.4	11.7	-0.6	-8.0	1.0	0.8	2.2	2.3	-4.2	2.4	1.5	1.2	1.3	1.1	1.0	1.0	1.0
Real Priv.Consump. per capita growth rate	-1.6	0.7	8.3	-2.9	-11.8	4.4	0.9	17.4	-0.2	-4.2	3.6	1.9	1.5	0.0	-0.6	-0.6	0.1	-1.1
Long-term public DOD 2_/ (in $ millions)	959.0	1002.8	1234.6	1494.7	1829.1	1977.0	2456.4	3067.6	3299.2	3394.5	3598.0	3659.5	3771.0	3910.5	4080.7	4303.6	4572.8	4862.3
LT public DOD/Exports goods & serv. 8_/	106.9	94.0	127.8	145.5	158.3	233.1	233.9	243.4	240.8	231.3	228.6	212.8	201.4	191.3	182.8	175.5	169.0	163.2
LT public DOD/GDP	32.3	40.7	48.1	60.6	65.8	77.1	65.7	66.7	66.2	68.0	67.1	64.2	62.2	60.7	58.9	57.8	56.4	55.4
LT public debt service ($ millions)	179.0	90.2	48.1	56.9	83.8	98.2	207.4	273.9	349.7	402.9	381.8	394.5	380.2	334.6	330.8	295.3	274.9	254.1
LT public Debt service/Exports GNS 8_/	19.8	8.5	4.6	5.5	8.7	10.2	19.8	21.7	25.5	27.4	24.3	22.9	19.2	16.4	14.8	12.0	10.2	8.5
LT public Debt service/GDP	6.0	3.7	1.7	2.3	3.6	3.4	5.5	6.0	7.0	8.1	7.1	6.9	5.9	5.2	4.8	4.0	3.4	2.9
LT public Interest/Exports GNS 8_/	6.3	3.9	3.5	4.0	5.3	4.9	9.2	8.9	9.3	9.9	8.6	7.3	6.0	5.1	4.4	3.8	3.4	3.0
LT public Interest/GDP	1.9	1.7	1.3	1.7	2.2	1.6	2.6	2.4	2.6	2.9	2.5	2.2	1.8	1.6	1.4	1.3	1.1	1.0
Gross investment/GDP	15.5	16.0	14.7	15.2	15.4	13.1	14.3	15.3	14.5	15.3	15.5	16.5	15.4	15.5	16.2	16.7	16.7	17.7
Domestic savings/GDP	-0.5	-1.7	1.7	3.1	6.4	2.5	8.9	6.2	7.1	9.1	8.6	8.3	7.9	8.2	9.0	9.7	10.4	12.1
National savings/GDP	-4.5	-8.6	-2.9	-1.9	0.5	-2.6	1.4	2.0	2.9	4.9	5.2	5.1	5.1	5.8	7.0	8.0	9.1	11.0
Marginal national savings rate (w.r.to GNP)	1.7	1.3	0.2	0.5	-0.5	-0.9	1.1	0.1	0.2	-1.5	0.1	0.0	0.0	0.2	0.4	0.3	0.4	0.6
Public investment/GDP	6.0	4.4	4.0	4.0	4.2	4.1	4.3	4.5	..	..	..	..	..	..	..	..	..	..
Public national savings/GDP	..	..	..	..	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Private investment/GDP	9.9	10.5	10.1	10.7	10.4	9.3	10.3	10.6	..	..	..	..	..	..	..	..	..	..
Private national savings/GDP	..	..	..	..	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Public/Private investment ratio	60.6	42.0	39.7	37.6	40.9	44.0	41.3	42.4	..	..	..	..	..	..	..	..	..	..
ICOR 3_/					5.4	4.0	9.2	7.8	5.4	5.0	4.9	4.9	4.7	5.0	3.9	4.2	4.3	4 4
Government revenue, excl.grants/GDP	21 1	20.7	19.4	19.4	19.4	18.3	18.1	18.2	16.8	17.5	18.2	18.8	19.4	19.4	19.4	19.4	19.4	19.4
Governmt expend.& net lending/GDP	30.2	31.0	27.6	26.6	24.6	22.6	21.3	20.8	20.0	21.0	20.3	19.1	17.8	18.0	18.3	18.4	18.2	18.1
Deficit (-) or Surplus (+)/GDP 7_/ (commitm basis, excl.grants)	-9.1	-10.6	-8.2	-7.2	-5.3	-4.2	-3.2	-2.6	-3.2	-3.5	-2.1	-0.3	1.6	1.4	1.2	1.1	1.2	1.3
Real growth rate of XGNFS 4_/	-4.8	9.1	4.8	9.8	-7.2	-12.7	5.0	12.6	5.5	-1.2	8.0	4.4	4.4	5.0	5.1	5.2	5.4	5.5
Exports GNFS/GDP 4_/	28.7	31.5	23.7	30.7	29.7	25.0	25.2	27.3	27.4	27.4	27.2	27.3	27.4	27.8	28 2	28.6	29.1	29.6
Real growth rate of MGNFS 4_/	7.6	15.3	-4.4	3.8	-9.3	-4.9	-5.2	45.3	-2.5	0.4	8.0	4.7	4.1	3.5	3.5	3.4	3.3	3.5
Imports GNFS/GDP 4_/	44.7	51.8	48.1	43.5	41.3	37.1	39.7	47.2	48 7	44.5	45.0	45.3	45.4	45.3	45.3	45.2	45.0	45.0
Current account balance ($ mill.) 5_/	-526.3	-638.6	-447.8	-445.4	-410.9	-450.4	-612.7	-470.3	-466.3	-431.3	-450.7	-481.5	-516.2	-524.1	-536.5	-546.5	-521.3	-495 1
Current account/GDP 5_/	-17.7	-25.9	-17.4	-18.1	-17.7	-17.6	-16.4	-10.2	-9.4	-8.6	-8.4	-8.5	-8.5	-8.1	-7.7	-7.3	-6.4	-5.6
Current account balance ($ mill.) 6_/	-396.1	-461.5	-265.6	-287.8	-272.3	-317.4	-410.7	-257.3	-263.3	-194.1	-199.4	-225.4	-266.3	-274.2	-286 6	-296.6	-271 4	-245 2
Current account/GDP 6_/	-13.0	-18.7	-10.3	-11.7	-11.7	-12.4	-11.0	-5.5	-5.3	-3.9	-3.7	-4.0	-4.4	-4.3	-4.1	-4.0	-3.3	-2.8
Merch. Terms of trade index (1980=100) (in US$ terms)	100.0	122.2	104.7	107.1	122.8	124.2	142.4	140.8	135.6	145.5	148.6	147.4	145.6	143.9	142.0	139.9	140.0	139.9

1_/ All figures are percentages, unless otherwise specified.
2_/ Public and publicly guaranteed debt outstanding and disbursed.
3_/ Five-year average, one year lag.
4_/ Derived from constant 1980 prices data (trade data from National Accounts for 1980-86; and from Balance of Payments for 1987-97).
5_/ Excluding official transfers.
6_/ Including official transfers.
7_/ Deficit or surplus on commitment basis.
8_/ Includes workers remittances

SENEGAL - BALANCE OF PAYMENTS

(US$ millions at Current Prices)

	Actual					Prelim.	Projections				
	1980	1983	1984	1985	1986	1987	1988	1989	1990	1992	1997
A. Exports of Goods & NFS	806.8	946.8	900.4	802.0	1027.0	1165.5	1271.1	1368.7	1463.6	1739.1	2811.5
1. Merchandise (FOB)	421.7	605.8	597.8	481.0	611.0	673.1	760.5	847.4	925.3	1120.1	1917.2
2. Non-Factor Services	385.1	341.0	302.6	321.0	416.0	492.3	510.7	521.3	538.3	618.9	894.3
B. Imports of Goods & NFS	1214.7	1291.9	1188.7	1128.0	1434.0	1448.0	1533.5	1592.1	1719.4	2081.1	3210.0
1. Merchandise (FOB)	875.1	917.3	818.9	790.0	1010.0	948.0	1009.4	1061.3	1146.0	1411.7	2246.4
2. Non-Factor Services	339.6	374.6	369.8	338.0	424.0	500.0	524.1	530.8	573.3	669.4	963.6
C. Resource Balance	-407.9	-345.1	-288.3	-321.0	-407.0	-277.5	-262.3	-223.4	-255.8	-342.0	-398.5
D. Net Factor Income	-98.6	-98.7	-122.9	-146.4	-231.7	-228.4	-237.4	-239.9	-227.8	-209.0	-141.1
1. Factor Receipts	23.7	25.5	15.7	13.6	17.3	20.0	20.1	20.1	27.9	39.6	76.4
2. Factor Payments	122.3	124.2	138.6	160.0	249.0	248.4	257.5	260.0	255.7	248.6	217.5
(interest payments)	57.0	41.3	51.6	42.9	97.7	115.8	130.4	149.0	138.4	116.4	90.2
E. Net Current Transfers (priv.)	-19.8	-1.6	0.3	17.0	26.0	30.6	31.4	32.1	32.9	34.7	44.6
1. Current Receipts	76.0	59.2	54.3	82.6	62.1	74.9	78.2	78.9	81.6	94.2	104.0
a. workers' remittances	74.8	55.1	50.4	32.2	..	74.9	78.2	78.9	81.6	94.2	104.0
b. other current trans.	1.0	4.1	3.9	50.4	..	0.0	0.0	0.0	0.0	0.0	0.0
2. Current Payments	95.8	60.8	54.0	65.6	36.1	44.3	46.8	46.8	48.7	59.4	59.4
F. Current Account Balance (excl.official transfers)	-526.3	-445.4	-410.9	-450.4	-612.7	-470.3	-468.3	-431.3	-450.7	-516.2	-495.1
G. Long-Term Capital Inflow	422.1	403.8	371.7	379.0	482.0	355.4	311.6	307.0	448.4	378.4	616.1
1. Direct Investment	12.9	-36.3	27.2	-3.3	-2.0	-54.6	-72.9	-18.1	4.0	25.2	56.7
2. Official Capital Grants	140.2	157.6	138.7	133.0	202.0	213.0	206.0	237.2	251.3	249.9	249.9
3. Net LT Loans (DRS data)	191.7	302.1	169.*	163.3	258.4	197.0	179.4	87.9	193.1	103.3	309.5
a. Disbursements	318.4	320.1	204.0	212.1	371.7	366.6	410.0	353.3	448.1	359.9	473.4
b. Repayments	126.7	18.0	34.7	48.8	113.3	169.6	230.6	265.3	255.0	256.6	163.9
4. Other LT Inflows (net)	77.3	-19.6	36.6	66.0	23.6	0.0	0.0	0.0	0.0	0.0	0.0
H. Total Other Items (net)	57.8	21.8	13.0	58.3	124.5	171.6	158.9	216.1	-15.0	0.0	0.0
1. Net Short Term Capital	83.5	36.3	29.8	91.7	51.7	0.0	-8.0	0.0	-15.0	0.0	0.0
2. Capital Flows N.E.I.	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
3. Errors and Omissions	-25.7	-14.4	-16.8	-33.4	72.8	171.6	166.9	216.1	0.0	0.0	0.0
OVERALL BALANCE (F+G+H)	-46.3	-19.7	-26.1	-13.1	-6.2	56.6	2.2	91.5	-17.3	-137.8	121.0
I. Changes in Net Reserves	46.3	19.7	26.2	13.1	6.2	-56.6	-2.2	-91.8	-91.4	-44.5	-140.5
1. Net Credit from IMF	37.2	12.6	4.2	40.3	6.2	-17.5	18.8	13.1	4.3	-40.9	-37.7
2. Other Reserve changes	9.2	7.1	22.0	-27.2	0.0	-39.1	-21.0	-104.9	-95.7	-3.7	-102.8
(- indicates increase)											
J. Additional financing required (gapfiller net of amortization and interest gaps)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	106.7	162.4	19.5

(Cont'd on next page)

SENEGAL - BALANCE OF PAYMENTS

(US$ millions at Current Prices)

	Actual					Prelim.	Projections				
	1980	1983	1984	1985	1986	1987	1988	1989	1990	1992	1997
Shares of GDP (Current US$):											
1. Resource Balance	-13.7	-14.0	-12.4	-12.5	-10.9	-6.0	-5.3	-4.5	-4.8	-5.6	-4.5
2. Total Interest Payments	1.9	1.7	2.2	1.7	2.6	2.5	2.6	3.0	2.6	1.9	1.0
3. Current Account Balance	-17.7	-18.1	-17.7	-17.6	-16.4	-10.2	-9.4	-8.6	-8.4	-8.5	-5.8
4. LT Capital Inflow (line G)	14.2	16.4	16.0	14.8	12.9	7.7	6.3	6.1	6.4	6.2	7.0
5. Net Credit from the IMF	1.5	0.5	0.2	1.6	0.2	-0.4	0.4	0.3	0.1	-0.7	-0.4
Memorandum Item:											
GDP (mill. of Current US$)	2970.0	2465.0	2324.0	2564.0	3740.0	4599.4	4979.7	4994.8	5356.7	6059.4	8816.8
Foreign Exchange Reserves:											
1. Int'l. Reserves (IFS 1ld)	8.0	12.2	3.7	5.1	9.4	9.2	---	---	---	---	---
2. Gold (end yr London price)	17.0	11.2	9.6	9.4	11.7	13.7	---	---	---	---	---
3. Gross Reserves incl. Gold	25.0	23.4	13.3	14.5	21.1	22.9	---	---	---	---	---
4. Gross Res. in Months Imports GNFS	0.2	0.2	0.1	0.2	0.2	0.2	---	---	---	---	---
Exchange Rates (CFAF/US$):											
1. Nom. Off. X-Rate (IFS rh)	211.3	381.1	437.0	449.3	346.3	300.5	---	---	---	---	---
2. Real Eff. X-Rate (1980=100)	100.0	92.0	94.0	103.0	112.0	106.0	---	---	---	---	---
3. X-Rate for GNP Conversion	211.3	381.1	437.0	449.3	346.3	300.5	---	---	---	---	---

STATUS OF WORLD BANK OPERATIONS IN SENEGAL

I. Statement of Bank Loans and IDA Credits (as of September 30, 1989)

Credit No.	Year	Borrower	Purpose	Bank	IDA	Undis-bursed
				Amount in US$ million (less cancellations)		
A. Thirty-nine (39) credits closed					420.57	
C11030-SEN	1981	SENEGAL	Forestry		9.30	2.42
C11760-SEN	1982	SENEGAL	Agricultural Research		19.50	0.74
C13100-SEN	1983	SENEGAL	Rural Health		15.00	3.68
CF0130-SEN	1984	SENEGAL	T.A. for Urban Mgmt & Rehab.		2.95	0.25
C13980-SEN	1284	SENEGAL	Parapublic II T.A.		11.00	1.05
C14060-SEN	1984	SENEGAL	Eastern Senegal Rural		16.10	5.11
C14590-SEN	1984	SENEGAL	Dakar Port III		2.65	0.82
C15540-SEN	1985	SENEGAL	Water Supply II		24.00	1.95
C17100-SEN	1986	SENEGAL	Energy Sector Rehab.		20.00	12.24
C17140-SEN	1986	SENEGAL	Telecoms II		22.00	17.08
C17350-SEN	1987	SENEGAL	Primary Education Dev.		12.00	9.11
C18550-SEN	1988	SENEGAL	Irrigation IV		33.60	29.23
C18680-SEN	1988	SENEGAL	Industry Sector		33.00	28.78
C18640-SEN	1988	SENEGAL	Municipal Housing Dev.		46.00	40.26
C19100-SEN	1988	SENEGAL	T.A. for Development Mgmt		17.00	13.65
C18021-SEN	1989	SENEGAL	SAL III		5.50	0
C19920-SEN	1989	SENEGAL	Small Rural Ops. II		16.10	13.37
B. Seventeen (17) ongoing credits					305.70	179.75
C. Twenty (20) Loans closed				129.33		
Total				129.33	726.27	
of which repaid				52.62	14.92	
Total held by Bank & IDA				76.71	711.35	
Amount sold	5.75					
of which repaid	3.26					
Total Undisbursed						179.76

II. Statement of IFC Investments (as of September 31, 1989)

Fiscal Year	Obligor	Type of Business	Loan	Equity Investment	Total
			Amount in US$ million		
1967	Societe Industrielle d'Engrais du Senegal (SIES)	Fertilizer Plant	2.45	1.01	3.46
1972-74	BUD Senegal	Vegetable Export	-	0.84	0.84
1974	SOFISEDIT	Development Finance Co.	-	0.34	0.34
1980	Banque de l'Habitat du Senegal	Money & Capital Market	-	0.46	0.46
1980	Societe Hoteliere du Barachois	Tourism	3.00	-	3.00
1982	Industries Chimiques du Senegal	Fertilizer Plant	25.00	-	25.00
1984	African Seafood	Fish Processing Plant	3.29	0.91	4.20
1986	SOTIBA-SIMPAFRIC	Print Manufacturing	3.20	-	3.20
1988	Industries Chimique du Senegal II	Fertilizer Plant	12.00	0.15	12.15
	Total Gross Commitments		48.94	3.71	52.65
	Less Cancellations, Terminations, Repayments, Sales and Losses		32.34	1.85	34.19
	Total Commitments held by IFC		16.60	1.86	18.46

SUPPLEMENTARY PROJECT DATA SHEET

TIMETABLE OF KEY EVENTS

(i)	Time taken to prepare the program:	28 months
(ii)	Initial discussions with IDA:	June 1987
(iii)	Appraisal mission:	June 15-30, 1989
(iv)	Negotiations:	November 2-3, 1989
(v)	Planned date of effectiveness:	December 1989

REFORM AREAS	STATUS	FSECAL ACTION PROGRAM	CONDITIONS FOR
	I. BANKING SECTOR REFORMS		
1. Bank Restructuring			
Purge private/semi-public banks of non-performing assets through write-offs or restructuring Liquidate public banks.	- USB has been liquidated, with sound assets taken over by Credit Lyonnais - Senegal in July 1989. Preliminary arrangements for BIAOS completed. The public banks were put in receivership in August 1989. A new bank is being created from viable assets of public banks. Non-performing assets of restructured or liquidated banks will be assigned to a recovery company.	-Arrangements with respect to functions of new bank and of recovery company (statutes, operating manuals, etc.) would be submitted to IDA for review.	Completed
		-Financial restructuring of BSK, MASSRAF and BIAOS would be completed.	Second Tranche
2. Financial Workouts			
Establish a viable fiancing scheme for write-off of non-performing assets and liquidation of public banks, with appropriate burden-sharing by Central Bank, Government and private shareholders.	-BCEAO agreed to a substantial increase in amounts of debt associated with restructuring to be consolidated, as well as to a major softening in terms (to 15 years with 3 years grace, at 3% interest) over conditions originally proposed. Budgetary impact of restructuring on Treasury agreed by IDA and government is sustainable.	-Government would be current in payment of annual liabilities incurred in restructuring.	Second Tranche
3. Divestiture			
Government will reduce its direct and indirect participation in all banks and financial institutions to 25 percent or below.	-Government's participation in USB/ Credit Lyonnais has been reduced from 62 to 5 percent, and in BIAO from 35 to 25 percent.	-Government's share in the new bank will be no more than 25 percent. Government's direct and indirect share in CNCAS and BICIS will be reduced to 25 percent.	Second Tranche

REFORM AREAS	STATUS	FSECAL ACTION PROGRAM	CONDITIONS FOR
4. Bad debt Recoveries			
Recoveries of bad debt (estimated at about 20% of total).	-Government has proposed to establish a recovery company which would have right to seize debtors' financial and material assets without going to court. Institution will be in place, with USAID-financed TA, by October 1989.	-Final determination of feasible schedule for, and total amounts of recoveries by independent audit	Completed
		-A Blue Ribbon Committee will be designated to review progress on debt recovery on an on-going basis.	Completed
		-An acceptable level of recoveries -- CFAF 9.8 billion by June, 1990 -- will be achieved following estimates of independent auditor.	Second Tranche
5. Cooperative Banking Structures			
The development of a grass-roots (cooperative/mutualist) system will be encouraged permitting the mobilization of small scale savings and access to credit SMES.	-The development of these grass-roots institutions will be encouraged through an appropriate legal and regulatory environment. USAID is promoting mutual credit schemes in the rural areas, and a CIDA TA project is aiming at the integration of the postal savings/checking with a broad-based mutualist structure.	-The TOR of a CIDA-financed technical assistance team which would work toward the establishment of a grass-roots network would be drawn up and agreed to.	Completed
		-An action program emanating from CIDA proposals would be agreed to.	Second Tranche
	II. BANK SUPERVISION		
1. Strengthening and Reforms of Bank Supervision and Control Mechanisms			
Upgrade Bank inspections and ensure follow-up of inspection reports. Update banking laws and regulations and develop uniform accounting system.	-BCEAO headquarters will reinforce its inspections and increase their periodicity. A regional banking commission is being established under the aegis of the BCEAO. BCEAO has begun a systematic review of banking laws to be upgraded and modernized. A uniform accounting system will be introduced.		

REFORM AREAS	STATUS	FSECAL ACTION PROGRAM	CONDITIONS FOR
	III. MACRO-LEVEL REFORMS (Senegal)		
1. Reform of Policies Directly Prejudicial to Sound Banking			
Policies common to UMOA but administered separately by Senegal and other member governments which have been prejudicial to health of the individual banks are to be removed.	-Abolition of targeted credit quotas agreed to by the Senegalese in advance of UMOA Council of Ministers decision to establish these guidelines taken in August 1989.		
	-The GOS has agreed to abolish all Government guarantees of domestic borrowing.	-Formal abolition by decree of September 10, 1989.	
	-Crop credits. Incentive for overborrowing will be materially reduced by abolition of TEP; BCEAO is requiring a clear financing plan (to cover eventual subsidies) for all crop marketing credits. In addition, Senegal is dropping all efforts to oblige banks to participate in crop credit consortia.	-Working of new crop credit system will have been reviewed in consultation with the APB and required corrective measures undertaken.	Second Tranche
	-Prior authorizations. The UMOA Council of Minsters endorsed both an increase in thresholds and a relaxation of current procedures. Moreover, application of the mechanism would no longer be associated with targeted credit guidelines.	-Functioning of the new system in Senegal would be reviewed and corrective measures would be taken. measures would be taken.	Second Tranche

REFORM AREAS	STATUS	FSECAL ACTION PROGRAM	CONDITIONS FOR
2. Reforms toward Improved Financial Intermediation			
Abolish bank-by-bank credit ceilings and replace by indirect instruments of monetary control (e.g. mandatory reserves). Phase in removal of 17% TPS tax on interest paid by borrowers.	-The UMOA Council of Ministers agreed to remove obstacles to the development of national interbank markets and ultimately to aim toward a "true" money (open) market operating on market-based principles.	-Agreement to a study on measures which would permit the elimination of bank-by-bank credit ceilings.	Completed
		-Consultation on the results of the study and agreement on procedures and timing for the introduction of market-oriented mechanisms.	Second Tranche
	-The Government successively reduced the TPS on interest paid to depositors from 17% to 7% to zero.	-Consultations before June 1990 on timing of abolition of TPS on loans.	
	IV. MACRO-LEVEL REFORMS (UMOA)		
1. Reforms toward Improved Financial Intermediation	Measures already taken		
Move toward market-oriented approach to monetary management in place of current system.	-Major shifts away from mechanisms emphasizing government (and BCEAO) leverage over lending decisions have taken place following the August, 1989 meetings of the UMOA Council of Ministers. Abolition of the preferential rate and the emphasis of the use of the money market an important step forward, as is the establishment of a new borrowing facility of last resort (TES). The effective widening of interest rate margins and their differentiation according to maturity also represents important changes. A shift toward a "true" money market system based on a tender-offer system for Central Bank money remains to be implemented.		

REFORM AREAS	STATUS	FSECAL ACTION PROGRAM	CONDITIONS FOR
	V. MACROECONOMIC STABILIZATION		
1. Ensure Macroeconomic Stability			
Continue to improve the Government's fiscal and current account opertions.	-Notable progress has been made in recent years such that the budget deficit went from 8.2% of GDP in 1982/83 to 1% of GDP in 1987/88. The inflation rate declined sharply.	-Ensure that the macro-economic program is on track to the satisfaction of the Bank. Judgement about macro-economic performance will be consistent with the annual PFP and on SAL IV, which is under preparation, if approved.	Second tranche

<u>ANNEX IV</u>

(Unofficial English translation of French original)

REPUBLIC OF SENEGAL

LETTER OF FINANCIAL SECTOR DEVELOPMENT POLICY

Dakar, November 3, 1989

INTRODUCTION

1. Confronted by a crisis affecting its banking system, the seriousness of which is evidenced by the accumulation of some CFAF 200 billion in non-performing assets out of a total asset base of CFAF 450 billion, the Government of Senegal has put into place a plan for the restructuring and reform of the financial sector. The motivations underlying this plan, as well as its objectives and modalities, first outlined in a document drawn up in October 1987 and amplified in two succeeding working memoranda, were confirmed in the directives of an Interministerial Council held on October 26, 1988. These documents were in turn discussed in meetings with an international donor group comprising the World Bank, France and the United States. Reforms of monetary policy instruments and BCEAO intervention rules undertaken within the monetary union (UMOA) complement the approach as applied in Senegal and constitute a framework which is more likely to ensure that the restructuring of the financial sector will be a lasting one and that improvements sought in financial intermediation will be achieved.

2. The principal measures which have already been undertaken or which remain to be implemented in order to carry out the reform program can be summarized as follows:

(a) rehabilitation and restructuring of the banking sector;

(b) orientations and actions of the Government with respect to the banking sector; and

(c) improvements in financial intermediation.

Part I: REHABILITATION AND RESTRUCTURING OF THE BANKING SECTOR

(i) Financial rehabilitation required

3. Generalized illiquidity and insolvency of eight of fifteen banks and two financial establishments resulting from the large volume of non-performing assets borne by these institutions led to increasing problems in cash management which could not be adequately dealt with by the series of ad hoc measures thus far applied. Thus various expedients such as Central Bank refinancing in excess of ceilings or of uncovered overdrafts, shifting of public deposits to weakened banks (or freezing existing deposits), refusal of access to clearing facilities, non-payment of tax liabilities to the Treasury, etc., did not resolve matters. Unsustainable Central Bank penalty rates on overdrafts, taken together with the large volume of unpaid liabilities, particularly to the Treasury, finally made it necessary to seek a more appropriate approach to the problem.

4. The decision taken by the BCEAO/UMOA to consolidate overdrafts and rediscounts of unviable paper over a ten-year period on the basis of bank workout plans represented a first step in this direction. However, the limitation of the proposed consolidations of liabilities solely to the

Central Bank, taken together with the high interest rate (6 percent) and shortness of the amortization period proposed meant that amounts to be consolidated were too small to deal adequately with the problem and the costs excessively high for the Government, which had accepted responsibility for them

5. It was thus that a deep and thoroughgoing financial rehabilitation program came to be seen as necessary.

(ii) Basic Principles

6. After numerous consultations with the bilateral and multilateral donors that had indicated their interest in supporting the sectoral program (World Bank, France and the United States), a rehabilitation plan was drawn up by the Senegalese authorities on the basis of the following principles:

-- purging bank balance sheets of bad debt (following capital write-off), through contributions of cash or concessional resources from shareholders, with the Government contributing in proportion to its shareholdings should the need arise; failing that, the assumption by the Government of bank liabilities to third parties (BCEAO, public and private depositors) not covered by sound assets, an approach which essentially covers banks owned in majority by the Government;

-- setting aside the financial resources necessary to carry out this operation while making sure that the total cost to the Government of taking responsibility for these liabilities -- particularly vis a vis the BCEAO -- remains within limits sustainable by the budget;

-- keeping alive only those financial institutions whose liquidity, solvency and profitability can assured from the beginning through splitting up, merger or downsizing;

These principles are implemented by:

(a) the mobilization of resources for the financing of bad debt, either

* through contributions by shareholders;

* through the consolidation by the BCEAO of claims arising from rediscounts or overdrafts;

* through the blocking of public deposits during the time it is expected to take to recover scheduled assets or for other resources to be released; or

* through concessional resources obtained by the Government to meet the expenses associated with restructuring, to wit:

** in the assumption of liabilities;

** through capital contributions to banks, to the limit implied by its share in their capital;

** the capitalization of new structures (e.g., banks established to take up the healthy portfolios of the USB and of the public banks); and

** the social costs associated with the restructuring.

(b) the splitting up of banks whose financial equilibrium cannot be guaranteed, with the good assets being transferred to a new bank and the non-performing ones being gathered into a recovery company.

(iii) Implementation

7. Begun several months ago, the rehabilitation of the financial sector has taken a number of different forms including:

-- the introduction of provisional measures

-- a scheme for a financial workout

-- restructuring of financial establishments in difficulty, namely in the public sector

(a) Provisional Measures

The power to grant new credits was withdrawn from banks with liquidity problems by denying them any increments over the credit ceilings fixed by the National Credit Committee under the aegis of the BCEAO. Moreover, a coordinator for the management and reorganization of the public banks was appointed in October 1988 with the role of these institutions being limited to holding operations. In October 1989 the mandate of the coordinator was extended to that of receiver of the establishments in question.

(b) Financial Workout Scheme

The financial workout scheme was established on the basis of the following elements:

-- For the financial institutions whose breakup is ordained (USB, BNDS, SOFISEDIT, SONABANQUE, SONAGA, ASSURBANK), financing requirements are set by the level of third party liabilities remaining with the liquidating structures together with the contributions of funds to be made to the new entities taking up the healthy portfolios remaining, against an equivalent amount of deposits.

Remaining liabilities not taken up amount to CFAF 88 billion (BCEAO), CFAF 51 billion (depositors) excluding refinancing of unbacked crop credits whose repayment is provided for in the Government's financial operations table (TOF), and CFAF 6.1 billion in debts to other creditors whose servicing is assumed by the Government.

-- For the other banks whose balance sheets can be restructured (BIAOS, BSK, MASSRAF), net financing requirements (possibly in the form of long-term loans on concessional terms) are determined by capital requirements after writeoff of existing capital against bad debts: CFAF 30 billion in total. In line with its share in total capital the Government is contributing CFAF 8 billion.

-- The financial workout scheme was developed in such a way as to limit the budgetary impact of the bank restructuring to about CFAF 10 billion per year during the initial years of the scheme. The costs in question are determined by the rates and maturities of the BCEAO consolidation, the repayment of the non-refinanceable element of the ONCAD claim, and the interest costs (at 8 percent) associated with temporarily blocked deposits.

-- Because of its size, the financing of the claim of the banking system on ex-ONCAD has been included in the workout but on a different basis. Amortization of the so-called 'non-refinanceable' element (CFAF 13 billion) is scheduled for a six-year period at a 7 percent interest rate while the 'financeable' element (CFAF 64 billion) will be included in the BCEAO consolidation package. These dispositions will have the effect of neutralizing the impact of this claim on the liquidity and profitability of the banking system as a whole.

8. The final workout financing scheme will have to be carried out according to the following arrangement, now ongoing, which has been accepted by the interested parties (BCEAO, donors):

-- Consolidation of outstanding Central Bank rediscounts, set at CFAF 126.6 billion by UMOA authorities -- of which CFAF 64 billion for ONCAD -- at 3% over 15 years with three years' grace;

-- consolidation by the banks which are already carrying the non-refinanceable element of the ONCAD loan -- CFAF 13 billion -- at a rate of 7 percent over six years;

-- blockage of deposit liabilities amounting to CFAF 50.7 billion, largely of the public sector, to be remunerated at 8 percent per annum and unblocked in line with bad debt recoveries, expected to amount to CFAF 32 billion over five years;

-- additional installments amounting to a total of CFAF 35 billion, to be paid by the Government over a three-year period.

9. Financing for the different commitments undertaken under the restructuring program is arranged as follows:

-- service payments for claims consolidated by BCEAO and the banks, as well as for interest rates on blocked deposits, are assumed by the Government and inscribed in the budget (TOF), with the total payments remaining within the above-noted limits. Following the stipulations of the consolidation agreements, payments will be debited from the account of the Treasury as they come due.

-- with respect to other public charges associated with the restructuring program, donor support has been sought:

* a 30-year loan, of which 10 years grace, for CFAF 11 billion has been obtained from the CCCE at a rate of 0.68 percent;

* the United States has agreed to contribute about CFAF 10 billion;

* support from IDA is being solicited in this connection. Counterpart funds associated with the credit would help the Government of Senegal to meet the costs associated with the restructuring and renewal of the banking system.

(c) Restructuring of Financial Institutions

10. The restructuring of financial institutions must be carried out in a way which reflects the modalities of the split-offs or rehabilitation programs and results in a reduction of the number of institutions and the absorption of restructured banks' bad debts into a financial establishment charged with recoveries. The influence of the Government must be reduced as well.

Bank rehabilitation operations

-- BIAOS: the rehabilitation plan put together in 1988 was successfully implemented. It provided for reductions in current costs, to be obtained from a retrenchment in personnel (175 employees) and compression of the branch network (closing of seven agencies); it also provided for the reconstitution of capital and well as an increase therein, to be subscribed by new shareholders. At the end of these operations the share of the Government in the total capital of CFAF 1.1 billion was reduced from 35 percent to 25 percent. With the bank's total capital rising to CFAF 1.5 billion the share of the of the Government will fall to 18.3 percent. Following an agreement with the BIAO group in June 1988 concerning the financing of non-performing assets, the Government contributed CFAF 500 million -- its share of the total -- beginning in June 1989. This amount was designed to make up the difference between the cost of the funds and that of a long-term concessional loan which will be put in place in 1989/90. The BIAO group has kept up its efforts to redress the cash position of BIAO and will confirm its support. The

Government of Senegal will renew its request to the BCEAO that it directly refinance the BIAO claim on ex-ONCAD.

-- Banque Senegalo-Koweitienne: The conclusions of the audit report on the accounts and financial situation of the bank were approved by the shareholders in January 1989. Provisions necessary for the coverage of loss risks on claims in suspense have been ascertained. A restructuring plan was worked out which provides for a reorganization of the bank's structure and for establishing methods and procedures of supervision under the oversight of an audit firm. The financial restructuring will be carried out through (a) an extinction of claims on one of the shareholder groups through the attachment of its real-estate holdings; (b) a capital increase; and (c) a grant of a line of liquidity on concessional terms.The Government will contribute 5 percent, in line with its share in total capital. An implementation schedule has been set which provides for the contribution of capital funds by the end of November 1989 at the latest. Failing that, the banking license will be withdrawn.

-- The Massraf Faysal al Islami Group: the conclusions of the second bank examination of BCEAO have been accepted and the absorption of the bank by its holding company has been authorized following the assumption by the Group of all losses. The Group has indicated its intention to rehabilitate the bank, which functions according to Islamic principles. A restructuring plan has been worked out; its timetable provides for the withdrawal of the banking license should injections of funds not be made by the end of November.

Split-off, merger, and recovery operations

-- With respect to USB, an agreement was reached with Credit Lyonnais on May 31, 1989 which permitted the absorption of the healthy part of the USB balance sheet by a new bank, Credit Lyonnais Senegal. This institution, with a CFAF 2 billion capital endowment 95 percent subscribed by Credit Lyonnais and 5 percent by the Government, began its operations on July 3, 1989, taking over some CFAF 13 billion in deposits against CFAF 7 billion in sound assets and CFAF 6 billion in cash equivalent. The bank is functioning with two branches and a staff of 125 persons. The USB obtained approval to lay off 155 employees and in the process of closing eight branches. The new institution has also become a recovery company and will be expected, in the longer term, to merge with that of the public sector.

-- After completion of the first phase of the assignment of the coordinator for the public banking sector (devoted to the evaluation of the financial situation of the different institutions) the principle involving the splitting up and merger of these banks has been accepted.

* The General Meetings of SONAGA, SONABANQUE, SOFISEDIT and ASSURBANK decided upon the advance dissolution of their institutions beginning on October 31, 1989. The decrees authorizing their dissolution, withdrawal of banking licenses and the nomination of receivers were issued by the Ministry of the Economy and of Finance.

* With respect to the BNDS, two-thirds of the total staff (323 employees) will have left the bank and received their severance payments on November 30, 1989. A decree naming a receiver under the terms provided for in article 68 of the Banking Law will have been taken before November 15, 1989, to go into effect January 1, 1990. On that date the BNDS will be transformed into a recovery company following the transfer of its sound assets to a new bank created simultaneously.

* The second phase of the coordinator's assignment involves the setting up of this new bank whose goal will, apart from taking over the sound assets of the liquidated institutions, be to provide banking services to small savers and to reach new categories of clients. The capital of the new bank will be open to private shareholders as well as to the insurance companies holding stock in ASSURBANK, through a stock swap. In any event, the Government's share will not exceed 25 percent. The New Bank will begin operations on January 1, 1990. It will limit its operations to the management of existing sound assets or their rollovers and to the collection of deposits until such time as new technical/financial partners have been found.

* Non-performing assets of the public sector banks will be merged together into the former BNDS, which will have been transformed into a recovery company. The new institution will also manage the deposits not assumed by the healthy institutions until these have been paid off. It will carry the BCEAO's consolidations of claims where assumed by the Government according to modalities still to be worked out with the BCEAO. Supplementary financial resources necessary to finance the other claims will be contributed to the recovery company by the Government. The recovery company will also undertake to recover the claims of those institutions which it absorbed, either by private agreement or through the court system: the former approach might take the form of consolidations of outstanding balances, equity loans or exchange of claims against shares. As long as appropriate resources can be found, financial support may be provided to reestablish businesses thought to be viable. The staff of the recovery company will be chosen from the personnel of the banks which it absorbed or from individuals hired on the basis of merit. The documents bearing upon the creation of the recovery company will be furnished to the donors. Under no circumstances will any eventual operating deficit be covered by public funds.

Part II: GOVERNMENT POLICIES AND MEASURES REGARDING THE BANKING SECTOR

11. Responsible for the regulation of the banking sector over which it has oversight, the Government exerted substantial weight on the banking system both as shareholder as well as direct and indirect borrower. In order to support sector rehabilitation a number of policy orientations in addition to the provision of financial resources have been adopted. These go in the direction of supporting (a) better banking supervision; (b) privatization; (c) measures facilitating bad debt recoveries; and (d) downsizing of staffing levels.

(a) Regulation and Supervision of the Banking System

A. Density of the Bank Network

12. Constituted by 15 banks and 7 financial establishments, the banking system of Senegal may give the impression of being relatively dense. Any evaluation of this question however, must take into account the diversity and activities of the overall banking structure and its components.

13. Whatever the case, a strongly restrictive position with respect to the licensing of new financial establishments has been taken by the Government, and any such licenses would be subject to joint consultations between the Government and the donors. The final goal is to arrive at a state of self-regulation, but without freezing monopoly positions. Up to the present the restructuring of the public sector banks now under way was to be carried out through the merger of four banks and one banking establishment into a single establishment. Obviously a more favorable stance toward new institutions will be taken with respect to mutualist organizations.

B. Supervision and Working Regulations of the Banks

14. The strengthening of supervision and the clarification of its organization must be obtained in parallel with the setting of more strict banking regulations. Some important decisions of principle in this direction were taken by the UMOA authorities in June and August 1989.

(i) Strengthening of Supervision

15. On site inspection: the BCEAO, which is responsible for on site inspection, has taken dispositions to reinforce its inspection services in order to increase the frequency of bank examinations carried out at its own initiative or in response to requests from national authorities. The principle of a maximum spacing (of 18 months) between inspections could be adopted.

16. Off site inspections: likewise carried out by the BCEAO on the basis of documents furnished periodically by the banks, off site inspections will be the responsibility of a specially designated bank inspection corps within the BCEAO. The establishment of a bank accounting

framework and a more frequent examination of bank inspection reports will increase the effectiveness of bank supervision.

(ii) Organization of Supervision

17. With the goal of strengthening oversight of banking activity within UMOA, the Council of Ministers of the Union decided to create a community-wide Banking Commission in the place of the national banking supervision commissions.

18. Composed of 16 members, with representation from each of the member governments, the Commission will have jurisdiction over banking supervision, ascertaining infractions and disposing of a consultative power with respect to all matters concerning bank regulations and their application. Its certified opinion will be required for all license applications and its power to revoke such licenses will be recognized.

19. The Commission will be appropriately endowed, particularly with respect to a permanent secretariat and a strengthened inspection service. Its establishment is set for October 1, 1990.

20. It must be noted that the Governor of the BCEAO retains the right to take, on his own initiative, restrictive action with respect to access to the operations and rediscounts of the BCEAO, for any bank in an irregular situation.

(iii) Working Regulations

21. Senegal indicates its agreement with respect to the strengthening of prudential regulations as proposed by UMOA authorities. At the same time it signifies its adhesion to the introduction into the banking regulations of rules of good conduct for shareholders and directors and to the enforcement of a common accounting framework. In any case Senegal will adopt, in conformity with article 22 of the UMOA treaty, uniform laws and regulations bearing upon the organization, functioning and activities of banks and financial establishments.

C. Government Disengagement

22. The parastatal banking sector, e.g., the establishments in which the Government holds shares (BNDS, USB, BICIS, BIAOS, BSK, BHS, BST, CNCAS, SOFISEDIT, SONAGA, SONABANQUE) grew through an accumulation of institutions and shares responding to diverse motives. With respect to this public presence, substantial but dispersed and lacking coherence, and leading to serious difficulties of several banks, an overall reorganization plan is being implemented on the basis of the following principles:

-- Government disengagement

-- Respect for management autonomy

(i) Government divestiture

23. In the spirit of the general policies applied for the reorganization of the public sector banks, a reduction of public shareholdings in the parastatal banks is to be achieved by bringing these shareholdings to 25 percent of total capital.

24. The process has already begun in the commercial banking sector: the share of the Government in the capital of BIAOS has already fallen from 35 percent to 25 percent; it will fall further to 18 percent after a call for new capital subscriptions. The modalities applied in the case of the USB, involving the creation of a new institution under the control of Credit Lyonnais have, by the same token, brought a reduction in Government representation from 62 percent to 5 percent. The divestiture by the Government of the capital of BICIS is to be begun by the end of January 1990. The minority shares held in the specialized institutions (BHS -- housing finance -- 9.09 percent, and CNCAS -- rural sector -- 28.2 percent) retain their justification because of the role of these institutions in supporting Government policies in the sectors in question. Nevertheless, the direct and indirect participation of the Government in the capital of CNCAS will be brought to the 25 percent ceiling through the sale of a part of Government-held shares, including those of the BNDS and of the USB, before June 30, 1990.

25. The public banking sector (in the sense of law 87-19 concerning the parastatal sector), made up of BNDS, SOFISEDIT, and the group SONAGA-SONABANQUE, has been profoundly transformed (cf. above).

26. The final share of the Government in the capital of the overall banking sector will be reduced to less than 10 percent as against more than 60 percent in 1987.

(ii) Autonomy of management

27. Besides the reduction in its shareholdings, "the Government will abstain from intervening in the management of the banks in such as to guarantee to the directors, freely chosen by qualified bodies, the autonomy of decision and the entire responsibility for their actions." (Presidential Directive no. 2 released by the Interministerial Council of October 28, 1988 on the restructuring of the banking system). As for the Government, it will make its choice for candidates for positions on the Boards of Directors following criteria based upon competence, experience and integrity.

28. In the same way, the management of the banking institutions will be carried out "in the respect of the norms of profitability and security" (ibid.).

D. Recourse to Bank Financing

29. The bad practices which permitted public bodies to maintain debit balances with banks have been abandoned; in any event these are prohibited by the rules of public accounting.

30. As for the direct obligations of the Government, these are limited to BCEAO advances which are statutorily limited to a ceiling of 20 percent of fiscal receipts. In order to limit the effects that this borrowing right may exercise on the financing of the private sector, new, restrictive dispositions have been fixed by UMOA authorities: inclusion of certain loans to the private sector into the calculation of the ceiling, and application of an interest rate close to that for ordinary credit.

31. The desire to avoid the excesses which may have taken place to the detriment of the quality of bank portfolios leads the Government of Senegal to renounce, unless specifically directed by legislation:

-- the provision of its guarantee favoring the domestic borrowings of public or private sector enterprises, on the pain of imputation to the Government's net borrowing position (position nette du gouvernement); grants of bank financing to public enterprises should be made following the usual criteria of profitability and solvency of the borrower;

-- the imposition on banks of an obligation to participate in financing packages put together at the initiative of public agencies, including the financing of crop marketing credits. The new principles underlying these financing arrangements which imply their unwinding upon maturing (cf. A-2 below), should permit the banks to participate in them without harm "to their financial equilibrium or to their profitability." (Presidential Directive no. 32, ibid.).

E. Objectives and Means of Recovery

32. The high level of frozen claims which has been ascertained justifies both a particular effort for recovery as well as the removal of obstacles that may hinder recovery procedures undertaken by the banks.

(i) Contribution of bad debt recoveries to sector rehabilitation

33. Bad debt recoveries enter into the workouts in providing financing totalling CFAF 32 billion for the rehabilitation of the banks in which the Government is intervening. The liberation of the blocked deposits of the public sector is dependent upon the realization of this objective.

34. In order to achieve the CFAF 32 billion target, the following measures are employed:

-- a survey of bad debts held by the troubled banks in such a way as to permit their grouping by debtor in order to provide a data base which could be used for cross checking against other sources (BCEAO Risk Center, arrears of the Treasury and of social bodies, etc.) This survey, which respects banking confidentiality, has been transferred to an agency for putting on computer file. The corresponding outstanding loans will be taken up by the Central Bank Risk Center under the names of the debtors, whether physical or moral persons, engaged directly or indirectly as guarantors or principal associates.

-- periodic survey of the efforts used for the recovery of claims (through legal means, direct settlements, etc.) by a Blue Ribbon committee attached to the Minister of Economy and Finance, to whom it will make quarterly reports of its observations and of the results obtained. The reports will be communicated to the donors. This supervision will apply to the recovery companies as well as to the banks undergoing restructuring.

(ii) Free access of the banks to legal recourse

35. Studies undertaken with the banks as well as findings made by a consultant have not indicated the need for profound changes in current legal dispositions as a means for ensuring the recovery of claims in suspense. However, all measures which might be necessary to this end-- particularly in view of the conclusions of the Blue Ribbon committee -- will be taken into consideration in order to stimulate the necessary reforms.

36. In conformity with the recommendations of the evaluation of recovery procedures just carried out, the Government will undertake to work together with the Professional Bankers' Association in order to summarize model agreements entered into with borrowers and to eliminate elements of imprecision that delay procedures (clauses bearing upon periodicity of accounts, imputation of interest, etc.).

37. With respect to the Government, it reaffirms 'its neutrality with respect to borrowers from banks ... which have complete latitude in pressing on with recoveries, whatever the rank and status of the borrowers.' (Presidential directive no. 23)

F. Social Measures in Support of Bank Personnel

38. After the restructuring of their accounts and portfolios, the financial situation of the banks in difficulty -- and even more the weakness of their real base of activity -- requires that their costs be reduced to the very limits of their operating conditions. To this end, a major downsizing of staffing levels has been undertaken: for the USB, 165 out of a total of 330 employees were taken on by Credit Lyonnais Senegal or kept by USB; in the public sector, 185 out of 545 employees will keep their jobs after restructuring. Taking account of measures already taken by BIAOS, the total cutback in jobs affected some 650 employees in the sector.

39. In order to soften the impact of job losses associated with bank restructuring, the following measures are planned:

-- to grant, to those affected by the restructuring, severance payments which are in excess of legally fixed amounts; and

-- easing their reemployment through the intervention of a specialized agency and through a facility providing for special access to concessional credits from the Reemployment Commission (Delegation a l'Insertion, a la Reinsertion et a l'Emploi).

40. These social costs have been taken into account in the financing scheme as it applies to the banks under the control of the Government. France has agreed to contribute an amount of CFAF 1 050 million in November 1989 under the 1989/90 structural adjustment loan of CFAF 11 250 million.

PART III: IMPROVEMENTS IN FINANCIAL INTERMEDIATION

41. To obtain not only a more certain supply of credit but an improvement in its allocation and to strengthen resource mobilization by financial institutions are objectives which are being sought in order to improve the functioning of the banking sector, and beyond that, the financing of the economy.

A. The Supply of Credit

(i) Monetary policy, management autonomy and bank profitability

42. Over the passage of time, certain monetary policy instruments (or use thereof) have either favored or at least accompanied the supply of bank credits which were poorly justified in economic terms, thereby also weakening the financial equilibrium of the banks called upon to make the loans.

43. However, the general framework of monetary policy is integrated with that of the UMOA, and follows common rules and objectives which constitute a constraint which is the counterpart of the zone-wide monetary solidarity that works to Senegal's advantage in particular.

44. It is precisely for this reason that a thoroughgoing review of the tools and policy orientations was launched at the initiative of the BCEAO, working in common with other institutions and donors. The review pointed up a number of shortcomings and weaknesses of the present mechanism, attested to by the serious difficulties of numerous banks as well as by excessive refinancing by the Central Bank.

45. Mid-course corrections or more profound reforms were brought to bear on the principal points of application of monetary policy: quantitative credit controls, sectoral allocations and interest rates.

(a) Quantitative credit controls

46. The restriction on the supply of credit through individual credit ceilings, instituted in 1980 to stem the deterioration of the external position, is applied individually to each financial establishment. The effects of this mechanism on the banks must be seen in relative terms considering that:

-- from a global perspective, outcomes were sometimes lower than the ceilings fixed for the year (exclusive of crop credits reclassified as normal credits, as in 1988);

-- the principles applied in the fixing of individual ceilings, which take account of the banks' cash positions as well as prior-year outcomes. No allocations are made to the detriment of non-performing banks, but on the contrary the system is structured to work in favor of the banks which are capable of financing healthy credits;

-- the inclusion, in the amounts which banks are permitted to lend each year, of foreign resources which might be effectively mobilized, particularly for social housing, agriculture, industrial restructuring and reemployment.

47. Working within the framework of monetary policy reforms ··ached within the UMOA structure, Senegal will support necessary changes i. he credit ceiling system in order to guarantee the competitive character of banking activity before a system of reserve requirements can be put in place.

(b) Sectoral Allocation of Credit

48. Usually justified on the grounds of scarce financial resources, sectoral credit policy is based on the idea of a responsible participation by the banks (at their risk) in the sectoral priorities fixed by the Government rather than being ruled exclusively by considerations of profit or the solvency of the borrower.

49. Applied on very empirical bases in the form of global sector objectives (rather than by individual establishment) this policy never permitted the attainment of the objectives which were sought, namely that nearly 70 percent of all credits be made for priority ends.

50. Under present circumstances the sectoral allocation policy no longer constitutes a constraint on banks' use of funds. In its session of February 9, 1989 the National Credit Committee formalized the abandonment of this policy and recommended the search for incentive measures favoring priority activities which would be neutral with respect of the autonomy of the banks. Such measures may be established once dispositions are taken at the UMOA level which go in the same direction.

(c) The Prior Authorization Procedure

51. This policy, which no longer has a raison d'etre as an instrument of sectoral credit policy, will continue to be applied as an instrument of control of the quality of paper against which Central Bank rediscounts are provided. In this spirit, a proposal will be made to the National Credit Committee before the end of December 1989 to:

-- raise substantially the current threshold of CFAF 70 million (to an amount permitting coverage of 50 percent of the number of beneficiaries and 50 percent of total amounts of lending might be studied); and

-- set a turnaround time as well as establish a standard request format.

(d) Interest Rates and Bank Margins

52. Interest rate levels, set within the framework of UMOA, will henceforth in large measure be set as a function the evolution of the cost of money on foreign markets. The Central Bank rates serve as a point of reference for the banks and are regulated for credits as well as for deposits:

* for credits, the reference rate is given by the discount rate plus a maximum of 5 percentage points;

* deposit rates are already free, with minimum rates being fixed for deposits above CFAF 500 million.

(e) Taxation of Lending Rates

53. The reduction of the TPS as applied to lending rates will be studied.

(ii) Crop Credit Financing

54. Although the Government is no longer directly involved as guarantor of crop credits, at least part of the cost burden from unwound deficits devolves upon it through the exercise of the groundnut guarantee fund or through the stabilization fund for other crops. From this viewpoint, directives drafted in September 1988 and confirmed in August 1989 by the UMOA authorities aim at the elimination of commercial and Central Bank financing of such deficits.

55. The general principle will be include crop credits under normal lending and Central Bank refinancing ceilings. This would imply:

* that crop credits would be included in the global credit ceiling which would likewise include advances to the Treasury;

* that crop credits will also be subject to the same conditions prevailing for other credits and will be subject to a reference rate equal to the BCEAO discount rate plus a maximum of 5 percentage points. Following the recommendations of studies on crop production and marketing activities, the Government is hoping that an interest subsidy fund can be set up in support of these activities;

* if the credit is refinanced by the Central Bank, the money market rate will apply for all such operations;

* the portion of the crop credit subject to Central Bank refinancing will be limited to 90 percent of the primary credit, which will require that the commercial banks carry 10 percent of such credits;

* in order to avoid both Central Bank financing of marketing deficits for specific crops as well as the failure to unwind or otherwise abuse such credits, crop credits must:

  ** be integrated into a global financing scheme which indicates how equilibrium in the financing of collection and marketing activities is to be achieved or provides for the coverage of any such deficits by means other than bank credits. What is aimed at is an equilibrium brought about through changes in producer prices or the mobilization of internal or external resources; and

  ** be authorized by the National Credit Committee and receive the agreement of the Board of Directors of the BCEAO to whom the financing scheme is submitted.

(iii) Access to Credit

56. This question arises for certain categories of borrowers or of Central Bank financing.

(a) Investment Financing

57. Investment financing by banks encounters the problem of scarcity of their long-term deposits and the weakness of their cash positions, which do not permit a major degree of term-transformation.

58. The mobilization and terms of a line of external credit from the World Bank (apex credit) represent an important change in this respect in that the apex credit permits banks to grant long-term credits (at their risk) destined to finance industrial modernization at a favorable rate of 9.5 percent without deviating in any exaggerated way from market conditions. In the same spirit, three banks have signed framework agreements with the CCCE for the refinancing, at 5 percent, for medium and long term loans.

59. Apart from the contribution of financial resources, such financing packages, in implying that the banks are in sound condition, also provide a certain assurance as to the appropriateness of the projects being financed and at the same time reduce the risks to the Treasury in case of non repayment. Analogous terms have been retained for reemployment financing under more concessional terms.

(b) Financing of Particular Activities and Lending Categories

Agriculture: the interventions of the CNCAS financed by its own (deposit) resources remain limited by CNCAS' cautiousness while needs are great (and risks high). In order to assess the possibility of a greater diffusion of credit in the rural areas, a study (provided for under SAL III) was undertaken with CCCE financing. Its terms of reference included both a comparison of agricultural credit programs set up under different auspices (agricultural extension firms, NGOs, etc.) as well as a definition of an action plan in respect of savings and credit. Its recommendations also aimed at the privatization of CNCAS the long-term evolution of its network into a mutualist system. These policy orientations will be incorporated into specific terms of reference.

Fishing: the creation of a mutual guarantee scheme, which has been studied with the support of the CCCE, seems to be feasible, but within a broader framework.

Housing: BHS financing is adapted to its needs but can no longer remain within the limits of deposit resources collected (apart from BCEAO financing) for mortgage financing. The measures envisaged in favor of savings will contribute to a desirable expansion of resources to finance a major demand.

SMEs/SMIs: the limits of financial support mechanisms utilizing public funds (interest rate subsidies, guarantee funds) necessitate the intervention of the commercial banks under their own responsibility but with the benefit of margins adapted to risk and monitoring procedures required for this type of loan. Modifications in regulations bearing on this point will be supported. Onlending of external lines of credit mobilized for the support of vocational reemployment has already been effected with a margin of eight percentage points for those banks that absorb the risk.

(c) Cost and Quality of Services

60. The bank restructuring program should permit an improvement in the quality and price of banking services. In this spirit, and in order to support competition, the interbank schedule of prices for banking services might be abolished.

B. Savings Mobilization

61. An ongoing objective, the strengthening of savings mobilization has inspired a set of dispositions aiming at improving remuneration of savings, broadening the deposit network and encouraging new financial instruments. However, the management of modest deposit liabilities requires special measures.

(a) Remuneration of Deposits

62. Rates: The regular increases in central UMOA rates have brought about the disappearance in the negative differential with external rates, it being necessary to remember that rates paid on large deposits are not limited by regulation. The ceiling on savings accounts (quasi-money) has been raised from CFAF 3 million to CFAF 6 million.

63. Fiscal measures: The service tax (TPS) on deposit rates, already lowered from 17 percent to 7 percent, has just been abolished; similarly, banks are generally exonerated from this tax for any increase in working resources constituted through borrowing. The fiscal statute bearing upon financial investments subject to specific taxation (IRCM or IRVM) and to general income taxes (IGR) will be reexamined.

(b) Network for Small Deposits and their Management

64. Bank restructuring may bring about a decline in the general mistrust vis-a-vis deposit accounts and the progressive implantation of the CNCAS could help bring bank services closer to those elements of the population hitherto untouched by the banking system.

65. On the other hand bank disaffection toward small depositors is growing, since the management of small accounts appears to be scarcely profitable if not costly.

66. The National Savings Fund and the (associated) postal checking system, in the process of being reorganized, could without doubt play a heightened role in this sector, traditionally their province. But the creation of a more dense network closer to the population in question would seem necessary to respond to their needs, and the coordinator for the reform of the public banking sector has been requested to study the conditions under which such a system could be created in such a way as to be viable and his expert-assistants have begun the preliminary work. Their investigations should be extended to seeking ways in which the modern financial sector could bridge the gap with the informal sector.

67. More generally, the authorities are in agreement with the establishment of mutualist savings and credit structures. Initiatives already undertaken on this score under the aegis of the Credit mutuel of France, USAID, women's associations, etc., are still in the stage of experimentation, which places them outside of the financial sector and its regulations (NGO statute). The position taken with respect to these experiments is to:

-- follow the activities being carried out (Ministry of the Economy and of Finance, Ministry of Rural Development and Ministry of Social Development), without exercising formal oversight but seeking to avoid excesses of a kind which could weaken their credibility or do damage to the public interest;

-- seek to appraise their results; and

-- take appropriate measures to permit their development in a framework which is adapted to the means and the role of those institutions which cannot be assigned to existing categories and which are called upon to service those strata of the population remaining outside the classical banking system. In this respect a federative system attached to a given financial institution might be envisaged, following the proposals made by the BCEAO.

Special technical assistance to the Ministry of the Economy and of Finance could be required to work out the details on such an organization, which appears to be the kind required to strengthen deposit mobilization and access to credit, as numerous experiences elsewhere have shown.

(c) Diversification of Savings Instruments

68. Some initiatives have been taken by commercial banks to diversify financial investment opportunities offered to the public, particularly through savings/credit schemes or through instruments which offer greater availability and confidentiality. In such cases banking and tax regulations and could be consequently modified within the limits required to support small savings.

69. The commitment to the program of privatization of public sector banks has likewise led to the examination of the possibility of investments in stocks and bonds. A study is to be undertaken under the aegis of the Commission for Reform of the Parastatal Sector in order to determine the size of a potential issue and subscription of stocks or bonds, as well as the assets required to set up an investment fund. The conditions for the creation of a trading corporation dealing with these securities must be identified, as must the role which the banks would be called upon to play in these operations.

Dakar, November 14, 1989

Ministry of the Economy and of Finance

PLAN OF ACTION FOR THE BANKING SECTOR

I. BANK RESTRUCTURING

BIAOS

- Signing of Protocol	JUNE	1988 A
- Presentation of Final Arrangement	DECEMBER	1989

BSK

- Presentation of Rehabilitation Plan	MARCH	1989 A
- Presentation of Final Arrangement	NOVEMBER	1989

MASSRAF

- Presentation of Rehabilitation Plan	JUNE	1989 A
- Presentation of Final Arrangement	NOVEMBER	1989

USB

- Signing of Protocol with Credit Lyonnais	MAI	1989 A
- Opening of Credit Lyonnais Senegal	JULY 3	1989 A
- Transformation into a Recovery Company	JULY	1989 A

PUBLIC SECTOR

- Naming of a Coordinator	DECEMBER	1988 A
- Naming of a Receiver	AUGUST	1989 A
- Agreement on Project for Establishment of a New Bank and Recovery Company	NOVEMBER	1989
- Establishment of New Bank	DECEMBER	1989
- Establishment of Recovery Company	DECEMBER	1989

MUTUAL CREDIT SECTOR

- Setting up of Technical Assistance Project	JANUARY	1990
- Institutional Studies		
* Launching	JANUARY	1990
* Action Plan	JUNE	1990

II. GOVERNMENT DISENGAGEMENT

- BICIS	JUNE	1990
- Sale of CNCAS shares	JUNE	1990

III. BAD DEBT RECOVERY

- Survey of Claims	NOVEMBER	1989 A
- Monitoring Procedures in Place	NOVEMBER	1989 A
- Recovery Targets		
(CFAF billion)		
* 4.0	DECEMBER	1989
* 9.8	JUNE	1990
* 14.5	DECEMBER	1990
* 19.2	JUNE	1991
* 23.4	DECEMBER	1991

IV. FINANCIAL POLICY MEASURES

- Formalization of the Abolition of Government Guarantees on Domestic Borrowing	AUGUST	1989 A
- Relaxation of Credit Ceiling System: Consultations (BCEAO, Donors)	JUNE	1990
- Changes in Prior Authorization Regime	DECEMBER	1989
- Abandonment of Targeted Credit	FEBRUARY	1989 A
- Consultations on Abandonment of Banking Services Cost Scale	JUNE	1990

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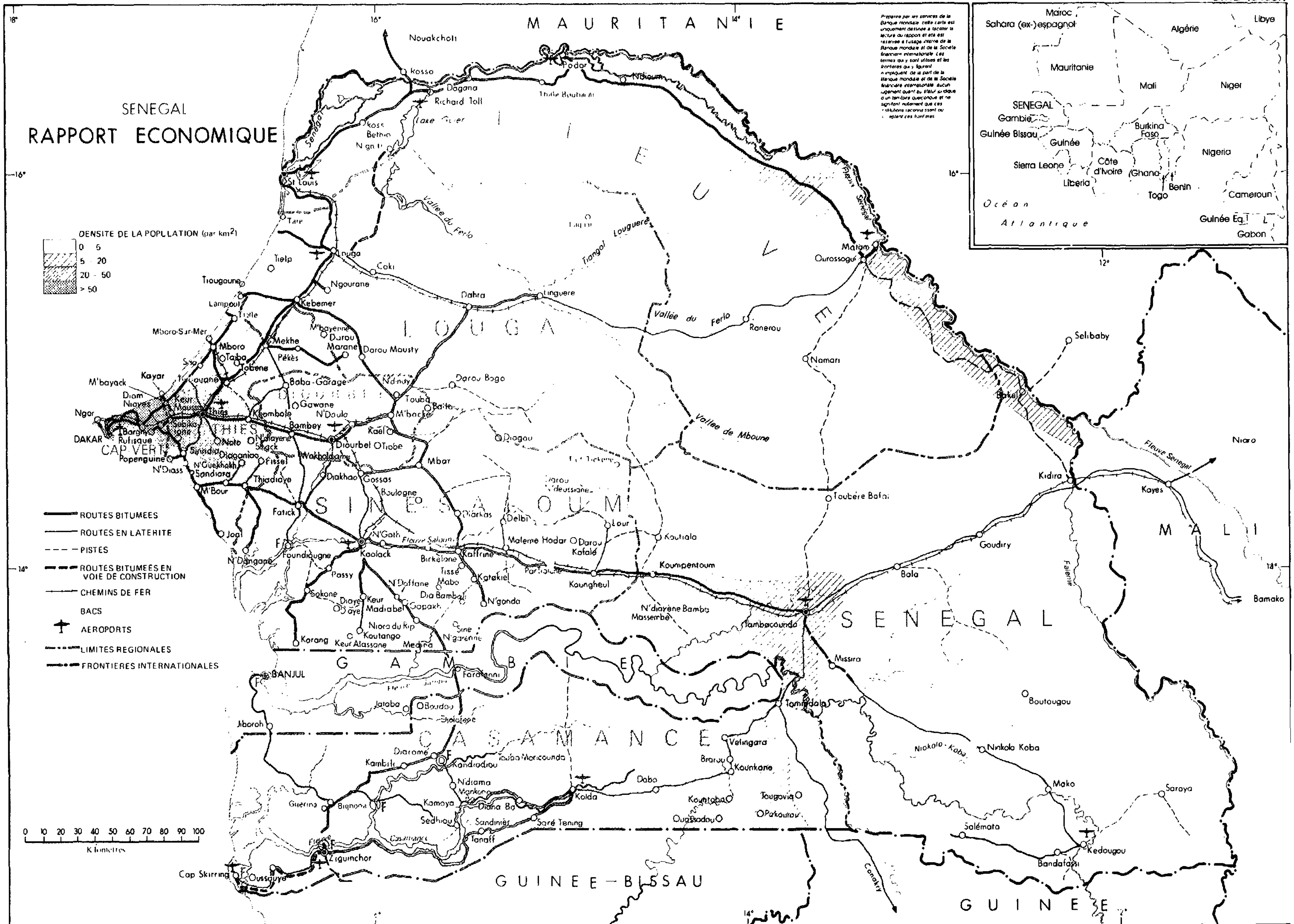

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