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REPORT AND RECOMMENDATION  
OF THE  
PRESIDENT OF THE  
INTERNATIONAL DEVELOPMENT ASSOCIATION  
TO THE  
EXECUTIVE DIRECTORS  
ON A PROPOSED DEVELOPMENT CREDIT  
OF SDR 11.9 MILLION  
AND A PROPOSED AFRICAN FACILITY CREDIT OF SDR 15.7 MILLION  
TO THE REPUBLIC OF CHAD  
FOR A FINANCIAL REHABILITATION PROGRAM

July 5, 1988

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## CURRENCY AND EQUIVALENT UNITS

|               |   |                        |
|---------------|---|------------------------|
| Currency Unit | = | CFA Franc (CFAF)       |
| US\$1.00      | = | CFAF 285.0 (June 1988) |
| CFAF 100      | = | US\$0.35               |

## FISCAL YEAR

January 1 - December 31

## SYSTEM OF WEIGHTS AND MEASURES: METRIC

### ABBREVIATIONS AND ACRONYMS

|            |   |
|------------|---|
| BEAC       | Banque des Etats d'Afrique Centrale                                       |
| CAA        | Caisse Autonome d'Amortissement   |
| CCCE       | Caisse Centrale de Coopération Economique                                 |
| CFAF       | Franc of the African Monetary Union                                       |
| COTONTCHAD | Société Cotonnière du Tchad   |
| CTT        | Coopérative des Transporteurs Tchadiens                                   |
| FAO        | Food and Agricultural Organization  |
| FIPP       | Fonds d'Intervention des Produits Pétroliers                              |
| FRC        | Financial Rehabilitation Credit   |
| FUA        | African Development Fund Units of Account                                 |
| IRCT       | Institut de Recherche du Coton et des Textiles Exotiques                  |
| MAGAVET    | Magasin Général d'Approvisionnement en Produits et Matériels Vétérinaires |
| MCT        | Manufacture des Cigarettes du Tchad                                       |
| NGO        | Non-Governmental Organization   |
| OFNAR      | Office National des Routes  |
| OMVSD      | Office de Mise en Valeur de Satégui-Déressia                              |
| ONDR       | Office National du Développement Rural                                    |
| ONPT       | Office National des Postes et Télécommunications                          |
| PFP        | Policy Framework Paper  |
| PHARMAT    | Centrale Pharmaceutique du Tchad  |
| SFA        | Structural Adjustment Facility  |
| SIMAT      | Société Industrielle de Matériel Agricole                                 |
| SONAPA     | Société Nationale de Production Animale                                   |
| SONASUT    | Société Nationale Sucrière  |
| SOTERA     | Société Tchadienne d'Exploitation des Ressources Animales                 |
| SR         | Saudi Rial  |
| STT        | Société Tchadienne de Textile   |
| TIT        | Société de Télécommunications Internationales du Tchad                    |

REPUBLIC OF CHAD  
FINANCIAL REHABILITATION CREDIT

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IBRD 21014

CHAD

FINANCIAL REHABILITATION CREDIT

CREDIT AND PROGRAM SUMMARY

Borrower: Republic of Chad

Beneficiaries: Republic of Chad and COTONTCHAD

Credit Amounts:

IDA: SDR 11.9 million (US\$16.2 million equivalent)  
African Facility: SDR 15.7 million (US\$21.3 million equivalent)

Terms: Standard IDA terms with 40 years maturity  
Standard SFA terms with 50 years maturity

Description: The proposed credit would support the first phase of the Government's adjustment program outlined in the Policy Framework Paper (1987-90). The principal objectives of this phase of the program are to improve resource use in two important areas of the economy: public finance and the cotton sector. The measures in public finance are designed to increase budgetary revenues, augment development-oriented current expenditures, and improve investment programming. The economic and financial viability of the cotton sector will be improved through measures to reduce costs of the cotton parastatal, improve extension and research, strengthen the sector's institutional set-up, and reform pricing policy. The program also aims to resolve the problem of COTONTCHAD's arrears to the banking system. In addition, the program includes studies to prepare future adjustment measures in public finance/administration, the public enterprise sector, and agriculture.

Benefits and Risks:

The main benefits of the financial rehabilitation program would be improvements in government revenues and expenditures, increased viability of the cotton sector in economic and financial terms, and an improved financial position of the public sector. The program would also strengthen the basis for higher economic growth in the medium term. As other operations in Chad, the program is subject to risks resulting from external factors (drought and renewed border conflicts) which could delay policy actions and absorb substantial government resources. Risks

(ii)

inherent in the program are that the Government might not be able to implement policy actions due to internal political resistance or that farmers' responses to cotton reform measures are not as anticipated. Efforts to reduce these risks to an acceptable level have been taken, e.g., by implementing the reforms gradually.

Financing Plan:

IDA US\$16.2 million equivalent  
SFA US\$21.3 million equivalent  
SJF US\$ 4.5 million equivalent  
ADF US\$38.3 million equivalent

Estimated  
Disbursement:

|               | <u>FY89</u>               | <u>FY90</u> |
|---------------|---------------------------|-------------|
|               | (US\$ million equivalent) |             |
| <u>Annual</u> | <u>21.0</u>               | <u>21.0</u> |
| IDA           | 4.0                       | 12.2        |
| SFA           | 12.5                      | 8.8         |
| SJF           | 4.5                       |             |

The credits would be disbursed in two tranches of US\$21 million equivalent each. The first tranche would be available upon effectiveness. The second tranche is expected to be disbursed about nine months later after the conditions for tranche release have been fulfilled.

Staff Appraisal  
Report:

Not applicable

Map:

IBRD 21014

**INTERNATIONAL DEVELOPMENT ASSOCIATION**

**REPORT AND RECOMMENDATION OF THE PRESIDENT  
TO THE EXECUTIVE DIRECTORS ON A PROPOSED DEVELOPMENT CREDIT  
AND A PROPOSED AFRICAN FACILITY CREDIT  
TO THE REPUBLIC OF CHAD FOR A  
FINANCIAL REHABILITATION PROGRAM**

1. I submit the following report and recommendation on a proposed development credit to the Republic of Chad in the amount of SDR 11.9 million (US\$16.2 million equivalent) for approval. The proposed credit would be on standard IDA terms with 40 years maturity and would help finance a financial rehabilitation program. It is proposed to supplement this credit with a credit of SDR 15.7 million (US\$21.3 million equivalent) from the Special Facility for Sub-Saharan Africa (the African Facility) established by resolution No. IDA 85-1, of May 21, 1985, and with special joint financing of SR17 million (US\$4.5 million equivalent) from the Saudi Fund. The program would be cofinanced by the African Development Fund through a credit of FUA 30 million (US\$38.3 million equivalent).

**I. THE ECONOMY**

2. The following assessment of the Chadian economy is based on the Country Economic Memorandum (Report No. 6785-CD) distributed to the Executive Directors in October 1987 and on missions that visited Chad in 1987 and 1988 to help the Government prepare its adjustment program. Annex I contains economic indicators.

**A. Background**

3. Although Chad has considerable agricultural and some mineral potential, its economic development has been hampered by a landlocked location, volatile climatic conditions, as well as periods of conflict for most of the time since its independence in 1960. Crop production and livestock account for nearly half of Chad's GDP and provide a living for 90% of its population of 5.2 million. Population growth is only 2.4%, and the balance of population to arable land remains quite favorable compared to other Sahelian countries. During periods of normal rainfall, Chad has been self-sufficient in cereals. Cotton and livestock are the main export products. Industry contributes about one-fifth of GDP and is dominated by a few large enterprises producing, apart from cotton, consumer goods for the domestic market.

4. Economic activity in the last 10 years has been severely disrupted by exogenous factors. In 1979-82, unrest escalated into a war during which GDP shrank by 30%. During the conflict, industries reduced or suspended operations, the banks closed down, public administration ceased to function, and much of the country's infrastructure was destroyed or deteriorated due to lack of maintenance. Economic recovery, which began with the establishment of the current Government in 1982, was again disrupted by a drought of unprecedented severity in 1984, followed by a sharp decline of the world market price for cotton. The border conflict with Libya continues and is absorbing substantial

resources of the country. Although, by 1986, real GDP had recovered to its 1977 level, it must be shared with one million more people. Per capita income, which has declined by 2% p.a. during the last 20 years, was only US\$140 in 1986. Socioeconomic indicators as well confirm that Chad is one of the world's poorest countries.

### B. Recent Economic Developments

5. Performance of the Chadian economy in the last few years was deeply affected by the crisis in the cotton sector. The price of cotton in CFAF fell by 67% from mid-1984 to mid-1986 due to a decline in the world market price and the depreciation of the US dollar. Moreover, the price decline coincided with a sharp increase in the expenditures of COTONTCHAD (the cotton parastatal), caused by inefficient management. As a result, the company sustained huge losses and accumulated arrears of CFAF 43 billion to the banking system. Despite the downturn in the cotton industry, Chad's remarkable rebound from the drought, with cereals production doubling, caused GDP to grow by 30% in 1985. In 1986, however, real GDP declined by 2% as the effects of the cotton crisis were felt more fully.

6. In response to the cotton crisis, the Government implemented a rigorous Emergency Program which aimed at reducing the sector's deficit. The program covered the 1986/87 and 1987/88 crop seasons and included the following measures: reducing input subsidies from 50% to zero over two years, limiting cotton production to 100,000 tons, closing redundant ginneries, exempting COTONTCHAD from payment of export taxes, and substantially reducing the staffs of COTONTCHAD and ONDR, the agricultural extension agency. The two-year program has achieved its objective: COTONTCHAD's costs were reduced from CFAF 913 per kg fiber in 1985/86, prior to the emergency program, to CFAF 544 per kg fiber in 1987/88. Cotton fiber is now being produced at about the same cost as in 1983/84, prior to the period of lax management, when COTONTCHAD's costs were roughly at the same level as those of other West African cotton companies. Its operating losses have been reduced from CFAF 19 billion in 1985/86 to approximately CFAF 5 billion in 1987/88. In 1986, the Central Bank of the Central African Monetary Union, of which Chad is a member, agreed to reschedule COTONTCHAD's arrears over a period of 10 years with 5 years grace and a two-year moratorium on the payment of interest.

7. Chad's already precarious public finances have been aggravated by the cotton crisis. The loss of export taxes on cotton, which was a major source of government revenue, contributed to a decline of nearly 20% in budgetary receipts in 1986. As a result, domestic resource mobilization through the government budget is now a very low 6% of GDP. To partially offset the loss of cotton revenue, the Government increased various consumer taxes. It also reduced current expenditures, which were already at a critically low level. Nevertheless, the fiscal deficit on current expenditures (commitment basis) increased from 1.6% of GDP in 1985 to 2.7% in 1986. The deficit was financed through budgetary aid and the accumulation of domestic and external arrears. The Government recognized the need to generate additional revenues through broadening the tax base and improving tax administration. In July 1987, as a first step, the cumbersome and complex system of taxing imports of petroleum products was replaced with a unitary consumption tax levied by the Customs services at entry points. Additional measures

were taken in November 1987 to improve collection of the new tax, and its yields are increasing.

8. Chad's external current account deficit increased sharply due mainly to the decline of world cotton prices and the weakening of the US dollar. With export earnings declining by 40% between 1984 and 1986, Chad's current account deficit almost doubled to 25% of GDP in 1985 and 1986. The deficit was financed by an increase of both capital grants and concessional lending. Over this period, the focus of aid also changed from emergency food aid to development assistance, which tripled between 1985 and 1987. Budget support also increased in response to the impact of the cotton crisis on public finances.

9. Although, by conventional measures, Chad has a relatively small external debt and a low debt service ratio, it has experienced serious debt-servicing problems. The country's external debt is equivalent to 25% of GDP; most of it is contracted by the public sector on concessional terms. In 1985 and 1986, Chad's scheduled debt service was only 7% of export earnings. Actual payments, however, covered only about half the debt service due, and arrears were accumulated which amounted to about US\$80 million by end-1986. The Chadian Government repaid arrears to most multilateral creditors and rescheduled arrears to bilateral creditors through negotiations. Scheduled debt service in 1987 and 1988 is in the order of US\$8-10 million, i.e., about 7% of export earnings. The servicing of the debt is constrained by inadequate public sector resource mobilization. In 1987, scheduled debt service amounted to nearly one-fifth of budget revenues and, thus, represented a heavy burden for Chad's public finances.

### C. Adjustment Policy Issues

10. Chad's economic growth in the next few years is hampered by a number of structural issues which mostly result from the country's low level of development. Among the most important adjustment issues are: (i) inefficiencies in public sector resource mobilization and expenditures as well as in public administration; (ii) restoring the competitiveness of the cotton sector; (iii) a pegged exchange rate which has increased the volatility of export earnings in local currency terms; (iv) an inefficient public enterprise sector; and (v) the rehabilitation of the banking sector.

11. Public Finance. Chad's public finances suffer from weak domestic resource mobilization, insufficient current expenditures, inadequate administration, and a severe debt service problem. The share of government revenue in GDP which already was very small has been further reduced by the cotton crisis. The challenge for the Government is to generate additional budgetary revenues and to raise civil administration expenditures to a level compatible with the requirements of the country's development strategy. In recent years, the Government has financed only current expenditures, with military spending and civil service salaries as the two biggest items; operating expenditures of development-oriented ministries have been slashed to the point where the Government is unable to carry out basic functions. Inadequacies exist in tax administration, and budget execution is characterized by much discretionary decision-making. Due to low budget revenues, Chad's public sector debt service is too high to be sustainable over the medium term, especially if the Government has to also ensure debt service on COTONTCHAD's arrears.

12. Future growth will require massive investment in infrastructure and human capital development. The Government is completely reliant on concessional external financing for its public investment program, as well as for a large portion of the associated recurrent costs. In recent years, public fixed capital formation has equaled about 8% of GDP. Domestic savings are highly negative, and the country has extremely limited access to private capital markets abroad. To use the available external resources effectively, the Government needs to define sectoral strategies and investment criteria, while emphasizing domestic resource mobilization through cost recovery schemes as well.

13. Cotton Sector. The Chadian economy depends heavily on the cotton sector for export earnings, government revenues, and farmers' cash income. Fundamental policy reforms are needed in the cotton sector in order to restore its competitiveness and to reduce the financial risks that result from fluctuations in the world market price. The efficiency of the cotton parastatal needs to be improved; measures are required to strengthen extension and research in the sector and to improve productivity at the farm level; and the pricing policy needs to be reformed to contribute to reestablish the financial viability of the sector. In addition, further study is needed to formulate a strategy for agricultural diversification with a view to reducing the predominance of the cotton sector.

14. Exchange Rate. As a member of the Central African Monetary Union, Chad cannot use the exchange rate to restore financial viability in the cotton sector and to improve the country's overall balance of payments position. The common currency of the Union, the CFA franc, is fully convertible into French francs at the rate of 50CFAF = 1FF, guaranteed by France. The Union also operates a common Central Bank (BEAC). In the last 15 years, exchange rate fluctuations vis-à-vis the US dollar played a larger role in destabilizing Chad's export earnings than changes in the world price of cotton. Under the Cotton Emergency Program, the donor community provided a de facto export subsidy by financing COTONTCHAD's operating deficits. In the absence of a flexible exchange rate policy, the need to step up efforts to improve the efficiency of the cotton sector is even stronger.

15. Public Enterprise Sector. The Chadian Government's use of public enterprises and market regulations to control economic activities has been fairly limited in the past. Many of the country's 40 public enterprises are plagued with inefficient operations and investments and have poor financial and administrative management. The accumulation of cross-arrears, particularly between the Government and the public utilities, has also become a major problem. The Chadian Government has no clearly-defined policy, legal framework, or institutional mechanism for evaluating and monitoring public enterprises. In addition, the Government has established a number of monopolies, mostly for public enterprises, and price controls on local production and imports. They have proven largely ineffective given the permeability of Chad's border and the existence of large informal markets. To the extent that these de jure controls do create distortions and inefficiencies, they will need to be progressively eliminated.

16. Rehabilitation of the Banking Sector. Since it resumed operations after the 1979-82 war, the banking sector has been constrained in its activities by two factors. First, a large share of

bank assets have been frozen since 1983 under a general bank moratorium. The moratorium was the result of the forced closing of the banking system in 1980 when the war prevented further operations; it is scheduled to expire at the end of 1988. Second, more than half of domestic credit has been absorbed by COTONTCHAD and is in arrears. The banking system, thus, has been unable to revolve funds lent previously and, under the rules of the Monetary Union, is constrained in expanding credit. The Government needs to assess the impact which the lifting of the moratorium in late 1988 will have on the banking system, and, as a priority measure to improve Chad's access to Central Bank credit, find a solution to COTONTCHAD's arrears.

## II. THE ADJUSTMENT PROGRAM

17. Objectives. In close cooperation with the Fund and the Bank, the Government prepared a Policy Framework Paper 1987-90 (SecM87-547), which the Executive Directors discussed on June 2, 1987. The overall objective of Chad's adjustment program, as described in the PFP, is to alleviate the economy's structural constraints on growth while containing the external and internal imbalances. The program aims at restoring modest economic growth and laying the foundation for more rapid growth in the 1990s by improving resource use in the public and private sectors through appropriate policy design and strengthened economic management. Policy improvements are needed in public finance, agriculture, livestock, the public enterprise sector, the banking system, and the industrial sector, to mention only the sectors that have the most immediate impact on growth. The principal quantitative targets of the adjustment program for the 1987-90 period are to: (i) achieve an average GDP growth of 2% in real terms per annum; (ii) keep the rate of inflation below 5%; (iii) contain the current account deficit (including grants) to 10% of GDP; and (iv) limit the overall balance of payments deficit to an average of SDR 2 million per annum, i.e., 10% of the 1985-86 deficits.

18. Adjustment Program for 1987/88. The PFP objectives in public finance have been translated into specific policy measures which are supported through a first-year IMF Structural Adjustment Facility (July 1987-June 1988). The program includes measures to: (i) increase revenues by introducing the new system for taxing petroleum consumption mentioned above; (ii) restrain the growth of expenditures through the application of strict budgetary controls, the integration of certain extra-budgetary revenues and expenditures into general Treasury accounting and limiting recruitment of civil servants; (iii) reduce domestic arrears and prevent the accumulation of new ones; and (iv) improve external debt management with respect to both borrowing and debt service payment. The Government's financial operations were consolidated by incorporating, for the first time, both current and capital expenditures in the 1988 budget. The program also includes measures aimed at the financial rehabilitation of COTONTCHAD and measures to pursue cautious credit policies.

19. Sectoral adjustment. In addition to reforms in public finance and in the cotton sector, the Government has also introduced policy reforms in two other important sectors, transport and livestock. In transportation, the Government has formulated a sector strategy and an investment program for 1988-93 which were presented at a sectoral donor meeting held in N'Djamena in February 1988. The new strategy focuses on: (i) the completion of rehabilitation and maintenance of the high

priority road network; (ii) continued strengthening of sector institutions, in particular their planning and management capacity; (iii) continued improvement of road maintenance financing; (iv) basic air transport services, and (v) promotion of private participation in the transport sector. In the livestock sector, a policy reform program has been adopted which, together with rehabilitation of infrastructure and institution building, aims at increasing the national livestock production on a sustainable basis and improving livestock marketing. The export regime is being reformed through the elimination of export quotas and of the export monopoly of a parastatal, SOTERA; cost recovery for veterinary services will be introduced, and the importation and distribution of veterinary products will be liberalized.

### III. THE FINANCIAL REHABILITATION PROGRAM 1988-89

20. Within the framework of the PFP, the next phase of the reform program, which the proposed IDA credit would support, aims at further improving resource use in two important areas of the economy: public finance and the cotton sector. The program would also include studies to deepen the reform process and to extend it to other sectors of the economy in subsequent phases of adjustment. Such a phased approach allows the Government to address the most urgent structural problems rapidly while reform measures in other areas are under preparation. The program takes into account the limited capability of the Chadian administration to prepare and implement policy reform programs as well as the need to identify measures in other areas. A UNDP-financed, Bank-executed Technical Assistance Project, provides assistance to the Government for the preparation and implementation of the reform program; an IDA-financed Economic and Financial Management Project (Credit 1872-CD) will provide additional support. The content of the financial rehabilitation program is described in the Government's Statement of Development Policy in Annex III and is discussed below. The specific actions to be supported by the proposed credit and their timing are summarized in Annex IV.

#### A. Public Sector Resource Management

21. Public sector resource management is one of the key tools for influencing economic activity in Chad. Increasing efficiency in the mobilization and use of public sector resources is therefore a central component of the Financial Rehabilitation Program. To this end, the Government's program includes: (i) reforms of the tax system; (ii) initial steps to restructure current expenditures; (iii) a rationalization of the public investment program; and (iv) the formulation of a public sector financing plan which reflects all these measures as well as the cotton sector reform program described below. This program aims at making more efficient use of public sector resources, thereby allowing the Government to extend the provision of basic services to the population.

#### Tax System

22. Chad's tax base is small relative to the size of the economy. In 1987, tax revenues accounted for only 6% of GDP, compared with 12% in the pre-war period (1973-75) and an average of 18% for other low-income African countries. Chad's low level of development and extremely narrow industrial base largely explain the low tax yields. Inadequate

tax administration compounds the problem. The bulk of tax revenues are generated through import duties and "unitary" taxes on domestic production, but this has jeopardized the viability of the few existing industries and has often increased smuggling rather than revenues. In recent years, the crisis in the cotton sector has aggravated Chad's fiscal problems. Historically, export duties on cotton have made up about 20% of tax revenues. In 1986, as part of the Cotton Emergency Program, COTONTCHAD was exempt from paying export duties; this put increased pressure on an already weak fiscal system.

23. The reform program includes short- and medium-term measures to increase tax yields and strengthen tax administration. To offset at least partially the loss of cotton export revenues, additional taxes were introduced in October 1986 on selected manufactured imported goods. Their yield, however, was small due to the inability of the tax administration to ensure adequate coverage of the tax base. In the short run, a reform of the cumbersome and complex system of taxing petroleum imports was the only source which could yield substantial additional revenue. In July 1987, a unitary consumption tax, which is levied by the customs service at entry points, replaced the existing petroleum tax system. In November 1987, the Government took additional measures to strengthen administration of the new system. Figures for the first five months of the new system indicate that the potential yield (tax assessment) of the new petroleum tax is close to the target (CFAF 4.5 billion over twelve months) set under the IMF's SFA program. It is expected that tax revenues from petroleum products, which made up 7.5% of tax revenues in 1987, will account for 19% of 1988 tax revenues.

24. While the measures described above are important, government expenditure needs and the limited scope for taxing the cotton sector during the adjustment period make it imperative to find new sources of revenue. The Government has decided to conduct a wide-ranging tax policy review and has requested IMF assistance. The review would include: (i) the tax administration system; (ii) extra-budgetary funds; and (iii) the scope for expanding the tax base. The study is scheduled for 1988, and the Government plans to start implementing reforms recommended by the study with its 1989 budget.

#### Public Investment Program

25. In the last two years, the Government has made significant progress in preparing a public investment program that reflects the economic priorities of the country. The progress to date is all the more remarkable since Chad has not had a formal public investment program since 1975. In 1986, the Government prepared an inventory of externally funded projects, which served as a basis for the preparation of the 1987 public investment program. The public investment program for 1988, which includes all donor-financed projects, for the first time has been incorporated in the government budget. The Government is committed to preparing a three-year rolling public investment program for 1989-91. This program will be reviewed by IDA, and it will be updated and extended annually.

26. Overall, the 1988 public investment program conforms to the Government's development priorities. The size of the investment program seems appropriate in view of the continued large reconstruction needs of the country. Assuming an implementation rate of 80%, the investment program is equivalent to 17.4% of GDP; fixed investment equals about 8%

of GDP; the difference is accounted for by external funding for operating expenditures of development projects, technical assistance, and training. The sectoral allocation emphasizes agriculture/livestock and transport infrastructure which each account for 29% of the total; industry/energy account for 24%, human resources for 12% and general development support for 6%. The public investment program is almost fully funded by external assistance. About two-thirds of the 1988 investment program is financed from grants and one-third from concessional loans on IDA-comparable terms.

27. The Government also has taken steps to strengthen public investment programming. It has issued a set of criteria for evaluating project proposals. In addition, the Government is formulating sectoral strategies which will serve as the basis for preparing future projects. Strategies for agriculture, livestock, and transport have already been formulated; a strategy for the education sector will be completed in late 1988, and work on a health strategy is envisaged for 1989. The Government will continue to use the strategies as a basis for aid coordination; an education sector donor meeting is planned in 1989.

#### Current Expenditures

28. The Government recognizes the need to reform its current expenditure system. The level of current expenditures is low, and their structure is flawed by serious imbalances. Personnel expenditures show the Government's resource constraints: most civil servants receive only 60% of their 1967 salary base. The most pronounced imbalance in the budget is reflected in the exceedingly small share devoted to non-personnel operating expenditures. In addition, budgetary control procedures are heavy. Under the financial rehabilitation program, the Government is starting to address these issues. As a priority, it is increasing operating expenditures of key development ministries; streamlining of budgetary procedures has been initiated, and a study of the civil service system will be undertaken to prepare future reforms.

29. Non-personnel Operating Expenditures. The Government's non-personnel operating budget, i.e., expenditures for materials and supplies, has been particularly constrained in recent years. It has been shrinking steadily both in absolute amount and as a proportion of the total budget. In 1987, the non-personnel operating budget showed a 54% reduction over the previous year; in 1988, it was reduced by a further 35%. Its share in the total government budget declined from 41% in 1986 to 20% in 1988.

30. These cuts have hit especially hard eight ministries central to development, i.e., the Ministries of Education, Public Health, Social Affairs, Agriculture, Livestock, Transport, Public Works, and Tourism/Environment. Their non-personnel operating budgets were reduced by 27% in 1986 and a further 63% in 1987. In 1988, allocations for these ministries make up only 11% of the total non-personnel operating budget. Moreover, actual expenditures are much lower than budget figures indicate, as military expenditures have been given priority reflecting continued security problems. Since 1985, only 20-50% of the allocations for non-personnel operating expenditures for these ministries have been authorized for payment; and the approved amounts represent only 3% of the total non-personnel operating budget. Actual expenditures, which are not broken down by ministry, are even lower. They are now so low that administrators lack basic office supplies, extension agents have no

means of transportation, health workers have no medicine to distribute, and teachers lack pedagogic materials. The Government urgently needs to raise these expenditures in order to restore administrative functions and to deliver basic services in agriculture and the social sectors.

31. Under the adjustment program, the Government is committed to increasing the expenditures for materials and supplies of these eight ministries. In 1988, budget execution for these ministries will follow more closely the initial budget allocation, and their non-personnel expenditures will be increased by CFAF 1.5 billion, thus restoring them to their level before the recent cuts. Revised budgets for the eight ministries have been prepared for the second half of 1988 incorporating the supplemental expenditures. The allocations for the social sectors have been increased as a priority. The revisions will be consolidated into an amendment to the 1988 budget to be adopted in July 1988. In 1989, operating expenditures for seven of the eight ministries will be maintained at that level and financed under the program. The 1989 increment for the Ministry of Livestock will be financed by the National Livestock Project, approved by the Executive Directors in May 1988. The detailed programming of the 1989 budget increase will be undertaken within the normal budget preparation process.

32. Expenditure Procedures. The existing expenditure authorization procedures do provide most of the information needed for monitoring the implementation of the operating expenditure increase. The Government will prepare, twice per year, detailed progress reports on the implementation of the operating expenditure increase. The reports will be countersigned by the Central Treasury, the Budget Director and by the technical Ministry concerned. They will include, for each of the eight ministries, the following information: the augmented budget allocation (i.e., the initial allocation plus the operating expenditure increase) cumulative commitments, disbursements, and the balance between budget allocation and disbursements (i.e., the implementation rate). Execution of the operating budget by end-1988 will be reviewed with IDA.

33. The existing budget execution procedure is complex because of the number of steps involved in the strict control of expenditures. To simplify budget execution, the Government has begun streamlining the expenditure authorization procedure by eliminating steps and reducing the documentation required. The Government intends to further review the scope for improvements in the expenditure authorization process in agreement with the IMF.

34. Civil Service Study. The Government recognizes the need to address the issue of personnel expenditure on the basis of an overall public administration study. In the period following the war, a substantial number of civil servants returned to their positions, which led to an increase in the overall size of the civil service. Due to budgetary resource constraints and the priority of military expenditures, the Government has contained the level of the wage bill. The issues for the future are to improve the efficiency of the civil service by matching skills with tasks and to identify ways of increasing salaries within the budgetary constraints. The Government will conduct, with IDA assistance, a study on the civil service and public administration as a basis for preparing future policy reform in this area.

### Public Sector Financing Plan

35. Under the adjustment program, the Government has prepared a public sector financing plan, covering the period 1988-1989. The plan, presented in Table 1, provides an overview of the Government's expenditure priorities and the resources available to finance those expenditures. The numbers for 1988 reflect the Government budget and are consistent with the targets established under the SFA program for June 1987-July 1988. The Government has confirmed that it intends to implement the financial program which was established with the staff of the IMF through December 1988. This program, which is presented in Table 1, includes objectives for revenues, expenditures, and the consolidated budget deficit. Implementation of the 1988 budget program will be reviewed with the staffs of the Fund and the Bank. The 1989 projections in the financing plan are tentative at this stage and will be firmed up with the preparation of the budget for next year.

36. This first public sector financing plan includes only the government budget and the financing requirements of the largest public enterprise, COTONTCHAD. While the plan covers the most important public sector expenditures, it underestimates the overall financing requirements of the Chadian public sector since data are lacking for several items. First, the financing requirements of other public enterprises will be assessed through several studies and incorporated into the plan at a later stage. Second, counterpart funds required for externally-financed investment projects are currently estimated at CFAF 800 million in 1988 and CFAF 1800 million in 1989. A detailed review is underway and may yield higher financing needs for 1989.

37. Public sector expenditures are fully financed in 1988, but a gap of CFAF 4.6 billion would still exist in 1989 after the adjustment measures have been taken. In June 1988, donors indicated that additional non-project assistance may be forthcoming which would be sufficient to cover the 1989 financing gap. The Government has established the following expenditure priorities: highest priority is given to adequately funding the Government's current budget; second priority is to make adequate provisions for covering the operating deficit of COTONTCHAD; the third expenditure priority consists of reducing COTONTCHAD's arrears vis-à-vis the banking system. In the event of insufficient resources, expenditures would be adjusted by reducing the amount currently envisaged for repayment of COTONTCHAD's arrears.

TABLE 1  
CHAD: Public Sector Financing Plan, 1987-89  
(millions of CFAF)

|  | 1987<br>est. | 1988<br>1st sem. | 1988<br>2nd sem. | 1988     | 1989     |
|--|--------------|------------------|------------------|----------|----------|
| <b>CENTRAL GOVERNMENT</b>                                      |              |                  |                  |          |          |
| Revenues   | 19,497       | 9,825            | 12,591           | 22,216   | 24,325   |
| Expenditures   | 78,677       | 38,945           | 45,044           | 83,989   | 92,010   |
| Current expenditures   | 27,677       | 11,445           | 17,344           | 28,789   | 30,610   |
| operating expend. in 8 ministries 1/                           | 297          | 250              | 1,750            | 2,000    | n.a      |
| government budget  | 297          | 250              | 250              | 500      | n.a      |
| supplemental budget  | 0            | 0                | 1,500            | 1,500    | 1,165    |
| Capital expenditures   | 51,000       | 27,500           | 27,700           | 55,200   | 61,400   |
| pipeline projects  | 51,000       | 27,500           | 26,900           | 54,400   | 53,400   |
| new projects   | 0            | 0                | 0                | 0        | 6,200    |
| government counterpart funds                                   | 0            | 0                | 800              | 800      | 1800     |
| Variation in Central Government arrears                        | 502          | (943)            | (1,388)          | (2,331)  | (1,500)  |
| Teachers' salaries   | 13           | 0                | (230)            | (230)    | 0        |
| Other Internal   | 489          | (750)            | (1,158)          | (1,908)  | (1,500)  |
| External   | 0            | (193)            | 0                | (193)    | 0        |
| Central Government deficit<br>(on a cash basis)                | (58,678)     | (30,263)         | (33,841)         | (84,104) | (69,185) |
| <b>PUBLIC ENTERPRISES</b>                                      |              |                  |                  |          |          |
| COTONTCHAD operating deficit                                   | (4,109)      | (588)            | (589)            | (1,177)  | (6,932)  |
| Reduction in COTONTCHAD arrears                                | (7,700)      | (1,700)          | (9,318)          | (11,018) | (8,200)  |
| Combined Central Govt./COTONTCHAD deficit<br>(on a cash basis) | (70,487)     | (32,551)         | (43,746)         | (76,297) | (84,377) |
| <b>FINANCING</b>   |              |                  |                  |          |          |
| External   | 70,487       | 33,149           | 43,148           | 76,297   | 79,783   |
| Project assistance (PIP)                                       | 68,973       | 33,149           | 43,454           | 76,603   | 81,134   |
| pipeline projects  | 51,000       | 27,500           | 26,900           | 54,400   | 59,600   |
| new projects   | 51,000       | 27,500           | 26,900           | 54,400   | 53,400   |
| new projects   | 0            | 0                | 0                | 0        | 6,200    |
| Non-project assistance   | 18,418       | 6,123            | 17,028           | 23,151   | 22,634   |
| United States  | 1,609        | 750              | 750              | 1,500    | 1,631    |
| France   | 9,099        | 3,000            | 7,010            | 10,010   | 4,010    |
| Ministry of Cooperation  | 5,382        | 3,000            | 4,408            | 7,408    | n.a      |
| CCCE   | 3,717        | 0                | 2,602            | 2,602    | 4,010    |
| World Bank   | 1,600        | 0                | 6,500            | 6,500    | 6,782    |
| African Development Bank                                       | 0            | 0                | 1,268            | 1,268    | 7,841    |
| Netherlands  | 0            | 673              | 0                | 673      | 2,370    |
| European Economic Community                                    | 6,110        | 1,700            | 1,500            | 3,200    | n.a      |
| STABEX   | 4,410        | 1,700            | 1,500            | 3,200    | n.a      |
| Fifth EDF  | 1,700        | 0                | 0                | 0        | 0        |
| Repayment of ext. debt (incl. debt relief)                     | (445)        | (474)            | (474)            | (948)    | (1,100)  |
| Internal   | 1,514        | 0                | (306)            | (306)    | (1,351)  |
| Banking system   | 439          | 0                | (306)            | (306)    | (1,351)  |
| Non-banking system   | 1,075        | 0                | 0                | 0        | 0        |
| Financing Gap  | (0)          | (598)            | 598              | 0        | 4,594    |

1/ Development ministries targetted under the FRC include Public Health, Education, Social Affairs, Public Works, Transport, Agriculture, Tourism/Environment, and Livestock.

## B. Cotton Sector

### Restructuring of the Cotton Sector

38. The financial rehabilitation program includes a comprehensive plan for restructuring the cotton sector and restoring its financial viability. Building on the achievements of the Emergency Program which reduced costs and losses within the existing incentives system and institutional framework, the restructuring plan, covering 1988/89-1990/91, would introduce fundamental reforms in order to increase efficiency and reduce the financial risks of the cotton industry. The plan has three components: (i) a program to increase COTONTCHAD's efficiency, (ii) a cotton development program at the farm level, and (iii) a reform of the producer pricing system.

39. Program to increase COTONTCHAD's efficiency. The restructuring plan contains an ambitious set of measures for improving COTONTCHAD's efficiency. These measures aim at reducing unit costs by about 30% so that by 1990/91 COTONTCHAD would be performing at a level comparable to the most efficient West African cotton producers. Measures have been adopted to reduce variable costs by 16% and fixed costs by 38%. COTONTCHAD's technical performance is good. The primary source of its inefficiency is high fixed costs which account for 25% of its cost price and which are three times higher than in the most efficient West African companies. A key measure to reduce these costs and to improve COTONTCHAD's management is the transfer of its financial and administrative services from the capital city to Moundou, the site of its operations, 480 kilometers away by road. A detailed plan for the transfer has been prepared, and the transfer should be completed by May 1989. The consolidation of COTONTCHAD's activities at Moundou will permit a reorganization of the company as well as a reduction of administrative staff and overhead costs.

40. COTONTCHAD has adopted other measures to increase efficiency including a staff reduction and training program, actions to improve management, and a modest investment program. COTONTCHAD will reduce its staff by 10% (109 positions) over the next three years and undertake a training program which will enable Chadians to fill 15 of the current 29 technical assistant positions. The salary scale and benefits will be modified to reduce the disparity between professional staff and workers as well as between COTONTCHAD and other employers. Actions to improve COTONTCHAD's management will also be undertaken: the recently created management and budget office will be strengthened; a unit will be set up to monitor the import, storage, and distribution of agricultural inputs; management of the warehouse and purchasing service will be improved; and a study will prepare a coherent management system and computerization plan. COTONTCHAD has potential for increasing the profitability of its oil and soap production. By November 1988, it will prepare an action plan for reducing costs of the oil and soap factory and, by March 1989, it will define a commercial strategy appropriate for the rapidly changing oil and soap market. COTONTCHAD's modernization program will permit the expansion of the capacity of two of its six ginneries and the purchase of other new equipment. These investments are needed to accommodate the expected increase in production, to reduce costs and to improve the quality of cotton fiber. COTONTCHAD's commitments under the restructuring program are formalized in a contrat plan with Government which will be signed by August 1988. The

achievement of cost reductions will be closely monitored and external audits will be done annually.

41. Cotton Development program at the farm level. The second component of the restructuring plan includes measures to: (i) increase cotton production, (ii) raise productivity at the farm level, (iii) reorient the work programs of the extension (ONDR) and research (IRCT) agencies, (iv) strengthen coordination between COTONTCHAD, ONDR and IRCT, and (v) introduce a more reliable financing mechanism. The cotton development program aims at increasing farmers' income from cotton production over the medium term through a combination of measures to expand production and reduce costs. Farmers were negatively affected by the Emergency Program, which limited cotton production to 100,000 tons through administrative means (control of cotton seed and other inputs distributed); maintained the producer price at 100 CFAF/kg, a decline in real terms; and reduced input subsidies from 50% in 1985/86 to zero in 1987/88. Despite these unfavorable factors, cotton production increased from 90,000 tons in 1986/87 to 127,000 tons in 1987/88 in part due to favorable climatic conditions and the depressed market for cereals. Interviews with farmers and government agencies indicate that Chadian farmers want to grow more cotton and use more inputs than were made available to them under the Emergency Program.

42. The cotton development program provides for an increase in cotton production to 145,000 tons by 1990/91, a level which has been surpassed in 5 out of the last 20 seasons. The expansion would favor the western part of the cotton zone where processing and export costs are lowest and where cotton fiber quality is highest. It is expected that farmers will increase production despite a lowering of the floor price based on evidence in Chad and elsewhere that the producer price is not necessarily the key determinant of the level of cotton production. The following other factors are important as well: (i) a guaranteed market outlet for cotton at a price known in advance which is not the case for alternative crops; (ii) returns to farmer's labor; (iii) relative returns to cotton and food crop production; and (iv) climatic conditions and incidence of pests.

43. Measures to increase productivity at the farm level aim at maintaining and, eventually, increasing the profitability of cotton production. These measures include increased availability of purchased inputs, a reduction in their cost, and the introduction of new technical packages. COTONTCHAD will increase the availability of inputs starting with the 1989/90 season. The plan aims at increasing the area on which inputs are used from 50% in 1987/88 to 72% of the cotton area by 1990/91. This would permit farmers who did not have access to inputs in 1988/89, to double their net income in 1989/90 by using the standard input package. Measures are also being taken to reduce input costs. For the 1988/89 season, inputs cost 20% less than in 1987/88 because of favorable world market conditions. In 1989/90, farmers will be able to choose among four technical packages, two of which are less expensive than the standard package currently offered. In order to identify other means of reducing costs, IRCT is testing less expensive, non-patented fertilizers and insecticides. Input costs would be further reduced if COTONTCHAD succeeds in lowering transport costs which account for up to half the cost of imported inputs. In support of these measures to increase productivity, ONDR is promoting the use of animal traction through farmer training and a credit scheme for equipment.

44. To support the cotton development program, ONDR's and IRCT's objectives and work programs have been redefined. The research institute IRCT will pay more attention to developing techniques which provide good economic and financial returns to farmers. The extension agency, ONDR, will train farmers groups to take over from village level extension agents and COTONTCHAD administrative tasks such as: estimating quantities of inputs needed, distributing inputs, managing credit, organizing and doing primary marketing of cotton. There is excellent potential for the development of these groups in Chad, because there are many literate, young farmers in the villages. ONDR's village level extension staff will be reduced from 585 to 360 during the three-year program, and staff will be retrained to assume their new role of advisor of village groups. In order to improve their coordination, ONDR, IRCT, and COTONTCHAD have signed a formal agreement clarifying their respective responsibilities, in April 1988.

45. Under the program, adequate financing for ONDR's and IRCT's current operations would be provided out of the Government's budget. In the past, both agencies received substantial support from external donors, and, prior to the cotton crisis, COTONTCHAD paid them a levy based on the quantity of cotton produced. Currently, ONDR's and IRCT's operating expenditures are partly funded from external assistance, but ONDR's budget in particular has not been adequately financed. The Government has given its assurance that adequate provisions will be made in the 1988 and 1989 budgets for ONDR's and IRCT's financing requirements.

46. Reform of the producer pricing system. A new producer pricing policy is an essential feature of the adjustment program. Under the existing pricing system, cotton is purchased from farmers at a fixed price which is not linked to international market conditions and which, according to custom, can only be increased. Farmers are fully protected from world price decreases; on the other hand, they do not reap the financial benefits from up-swings in world prices. Since the producer price currently accounts for close to 50% of COTONTCHAD's total average production costs and 60% of its average variable costs, COTONTCHAD's ability to reduce costs to adjust to low world prices is severely limited at the current producer price of 100 CFAF/kg for the best quality cotton, and the risk of large deficits is high.

47. In the past, COTONTCHAD's operating deficits were to be financed by an independently managed cotton price stabilization fund (CAISTAB) which got its resources from transfers of 80% of COTONTCHAD's net profits. However, as in other African countries, the fund did not support the sector in times of collapsing international prices. It instead served as an instrument to tax the sector, and the accumulated resources were used to finance a variety of activities largely unrelated to the cotton industry. In addition, the past stabilization system did not provide incentives to COTONTCHAD to be efficient since its deficits were to be fully covered whether they stemmed from producer price supports or from high costs due to poor management. The weaknesses of the system were exposed in the cotton crisis when the increased volatility of world cotton and financial markets, combined with the high producer price, which had been increased from 60 CFAF/kg in 1980/81 to 100 CFAF/kg in 1984/85, resulted in large deficits. Due to the failure of CAISTAB, these deficits were financed by arrears to the banking system and by the donor community in the context of the Emergency Program.

**Table 2**  
**Cotton Restructuring Plan - Key Indicators for Pricing Policy 1/**  
**(CFAF/kg)**

|   | <u>Year 2</u>            | <u>Restructuring Plan</u> |                |                |
|---|--------------------------|---------------------------|----------------|----------------|
|   | <u>Emergency Program</u> | <u>1988/89</u>            | <u>1989/90</u> | <u>1990/91</u> |
| <b>Floor Price-Seed Cotton</b>                |                          |                           |                |                |
| 1st Quality (%= 98, 80, 82.5, 85)             | 100                      | 100                       | 90             | 90             |
| 2nd Quality (%= 0, 15, 12.5, 10)              | -                        | 75                        | 70             | 70             |
| 3rd Quality (%= 2, 5, 5, 5)                   | 40                       | 50                        | 45             | 45             |
| <b>Average Floor Price-Seed Cotton</b>        | 98.9                     | 93.8                      | 85.3           | 85.8           |
| <br><b><u>COTONTCHAD</u></b>                  |                          |                           |                |                |
| - Average Floor Price - Fiber (1)             | 260                      | 247                       | 220            | 211            |
| - Other Variable Costs (2)                    | 170                      | 167                       | 161            | 162            |
| - Total Variable Costs (1+2)                  | <u>430</u>               | <u>414</u>                | <u>381</u>     | <u>373</u>     |
| - Fixed Costs (3)<br>(excluding depreciation) | 60                       | 55                        | 43             | 35             |
| - Processing Costs (2+3)                      | 230                      | 222                       | 204            | 197            |
| - Total Cost (1+2+3) 2/                       | <u>490</u>               | <u>469</u>                | <u>424</u>     | <u>408</u>     |
| <br>Assumed World Price - Fiber 3/            | 380                      | 380                       | 380            | 380            |
| <br><b>COTONTCHAD's Deficit at this World</b> |                          |                           |                |                |
| Market Price                                  |                          |                           |                |                |
| - Per kg Fiber                                | 110                      | 89                        | 44             | 28             |
| - Total (billion CFAF)                        | 5.8                      | 3.9                       | 2.2            | 1.7            |
| <br><b><u>Memo Item</u></b>                   |                          |                           |                |                |
| Production of Fiber                           | 47,910                   | 43,600                    | 50,430         | 58,950         |

1/ In current prices.

2/ Inclusion of the depreciation allowance would add 20 CFAF/kg to COTONTCHAD's cost price in 1990/91.

3/ An assumed world price of 380 CFAF/kg fiber has been increased by 20 CFAF/kg to account for net revenues for oil and soap sales. This is a conservative hypothesis at the lower end of the price band of 330-550 CFAF/kg within which cotton prices have oscillated over the last 15 years. Under this hypothesis, COTONTCHAD's deficits would be equivalent to its fixed costs in 1989/90 and lower than fixed costs in 1990/91. However, world prices are expected to be higher than 380 CFAF/kg in these two years, meaning COTONTCHAD is likely to break even or generate a surplus.

48. The reform of producer pricing policy aims at minimizing financial risks of the Government and COTONTCHAD in the face of considerable uncertainty about world market prices, while protecting farmers' incomes and assuring that they benefit when world prices are high. The new pricing policy contains four elements: a price differential according to cotton quality, a floor price, a purchase price announced to farmers at planting time, and a price support fund. The price differential according to quality aims at encouraging farmers to sort their cotton by grade; this would improve the quality of ginned cotton. In 1988/89, a third quality will be introduced which is intermediate between the existing two grades.

49. In the new pricing system, the floor price would guarantee farmers a minimum return to cotton production irrespective of the short-term fluctuation of world prices. The floor price will be reduced from 100 CFAF/kg for the first grade cotton to a maximum of 90 CFAF/kg for the 1989/90 and 1990/91 seasons. Combined with other cost reductions mentioned above, this would lower COTONTCHAD's variable costs to about 380 CFAF/kg fiber. This reduction in variable costs under the adjustment program would justify an expansion of cotton production which would, in turn, result in lower unit fixed costs. Since even in years of low world prices revenues would be sufficient to cover variable costs, COTONTCHAD's deficits would be limited to its fixed costs (CFAF 2 billion CFAF in 1990/91). Hence, by reducing financial risks for COTONTCHAD and the Government, the new policy pricing policy would permit a sustainable increase in cotton production.

50. The element of flexibility in the new system is the purchase price which will be calculated in April of each year and announced to farmers in May/June, which is planting time. As mentioned above, the purchase price cannot be set lower than the floor price. However, if the world market price was more than sufficient to cover COTONTCHAD's variable and fixed costs (excluding depreciation) in the previous season, then a proportion of this surplus would be passed on to farmers through a higher purchase price in the season for which the price is being set. The balance of the surplus would be allocated between COTONTCHAD's depreciation allowance, the price support fund, and taxes. The detailed method for setting the purchase price and allocating the remaining surplus will be agreed upon with Government before November 1988. Farmers' reactions to the new policy will be closely monitored.

51. Under the reform program, a price support fund would be created within COTONTCHAD to finance the deficit arising from supporting the floor price. The new pricing system would substantially decrease the amount needed in the fund, and its joint management by COTONTCHAD and a representative of donors should improve accountability and provide the necessary incentive to use the resources for their intended purpose. The fund would be constituted from external financing under the adjustment program and would be replenished from a portion of the surplus between the world price and COTONTCHAD's cost. Clear guidelines will be developed for the constitution and operation of the fund before November 1988.

#### Settlement of COTONTCHAD's Arrears

52. COTONTCHAD accumulated CFAF 43 billion in arrears during the war and the cotton crisis; CFAF 42 billion have been rediscounted by the Central Bank, and the balance is held directly by the primary banks.

The arrears not only jeopardize COTONTCHAD's financial viability, they also present a problem for Chad's public finances and, under the rules of the monetary union, affect the availability of new credit to the economy. As mentioned in para 6, in 1986 the Central Bank rescheduled the CFAF 42 billion arrears over a ten-year period, with 5 years grace and a two-year moratorium on interest payments. This arrangement provided some time for the Government to seek a more sustainable solution for settling the arrears, before having to face service payments which substantially exceed the payment capacity of COTONTCHAD and the Government.

53. Under the terms of the rescheduling agreement with the Central Bank, COTONTCHAD is obliged to reduce its arrears by CFAF 11.1 billion before October 31, 1988. In accordance with the Government's commitments, COTONTCHAD repaid CFAF 7.7 billion by October 1987, and has made provisions to repay another CFAF 7.4 billion before October 31, 1988; this would bring the total arrears repayment to CFAF 15.1 billion by the end of October 1988, or CFAF 4 billion more than envisaged under the agreement with the Central Bank. These repayments were made possible by savings and receipts in excess of those anticipated in the financing plan of the Cotton Emergency Program. Taking into account the CFAF 3.8 billion interest accumulated during the moratorium, the total amount due to BEAC on October 31, 1988, is CFAF 30.6 billion.

54. Following a request of the Chadian authorities in May 1988, the Central Bank has proposed a freezing of CFAF 14.2 billion of COTONTCHAD's remaining arrears. The freeze would be in effect for at least five years, and no new interest charges would accumulate on these arrears. As part of this proposal, the Central Bank has asked the Government to repay CFAF 14.2 billion, which corresponds to the balance of principal, within a maximum period of two years. Discussions regarding the remaining interest due of CFAF 2.1 billion will take place later. This proposal was confirmed with representatives of the Central Bank during negotiations of the FRC.

55. The Government has confirmed its commitment to repay the Central Bank on the basis of such an arrears settlement program, on the condition that the other priority needs, (i.e., current expenditures of the Central Government and COTONTCHAD's operating expenditures) are met first. The public sector financing plan provides for the repayment in 1988 of CFAF 3.6 billion in addition to the CFAF 7.4 billion already scheduled under the Cotton Emergency Program. In 1989, CFAF 8.2 billion will be repaid, CFAF 7 billion of it to the Central Bank. In addition, CFAF 1.2 billion will be repaid to the commercial banks that extended loans to COTONTCHAD in 1985; this repayment will be funded through a special credit from the Caisse Centrale de Coopération Economique. The financing plan shows a deficit of CFAF 4.6 billion in 1989, which, in the absence of additional resources, would reduce repayment to the Central Bank from CFAF 7 billion to CFAF 2.4 billion.

### C. Preparation of Future Reforms

56. Reform measures under the financial rehabilitation program have been limited to the two areas in which changes are needed most urgently, while studies are being undertaken for preparing future phases of Chad's adjustment program. Studies identified thus far will address additional issues in public finance/administration and extend the preparation of adjustment measures to another important area of the

public sector, parastatals, as well as agricultural issues outside the cotton sector.

57. Public Enterprises. In the Policy Framework Paper, the Government indicated that it intends to initiate a public enterprise sector reform program. As preparatory steps for future policy reform, diagnostic studies of the most important public enterprises will be undertaken with financing from the Economic and Financial Management Project. These studies will provide the basis for deciding whether individual public enterprises/agencies should stay in the public sector because they provide an essential public service or are of strategic importance to Chad; be privatized, if they are basically viable; or be liquidated, if they are not viable. A first set of studies for five enterprises will be completed in 1988. Additional enterprises will be studied in a second phase. Another six enterprises are already being studied under other Bank operations or by other donors.

58. Reform of the public enterprise sector will also have to include the settlement of cross arrears among the parastatals, between them and the Government, and with the private sector. A study will be undertaken in 1988 to determine the extent of these cross arrears and to prepare proposals for eliminating them. In addition, a study of the banking sector is envisaged to prepare the lifting of the banking sector moratorium in late 1988 and to assess the need for policy reform. Terms of reference for the diagnostic studies and the cross arrears study were finalized during the FRC appraisal mission, and terms of reference for the banking sector study are under preparation. These studies will be funded available under the IDA-financed Economic and Financial Management Project.

59. Public Administration/Civil Service. As mentioned above, the Government will undertake a study of the civil service/public administration. Building on a civil service census which was completed in December 1987, the study should determine what functions are essential for the Government to perform within its resource constraints and how best to perform these functions, and should analyze the present administrative structure and government staffing. It would also make recommendations for changes in these areas and develop a public administration in-service training program. The study will be financed by the Economic and Financial Management Project. Implementation of the civil service/public administration reforms will take place in future phases of the adjustment program.

60. Agriculture. The Government has defined a development strategy for the agricultural sector, including livestock, fisheries and forestry, which was presented at a donors meeting in December 1986. In many areas, however, the existing knowledge was insufficient to define a detailed strategy and action plan. Two priority issues which require more analysis are food security and irrigation development. The Government is addressing them in collaboration with IDA and other donors. The need to collect new data and do in-depth analysis of specific areas and policy questions is also being addressed by the IDA-financed Agriculture Sector Rehabilitation Project (Credit No. 1775-CD). The project will assist in the design of detailed strategies and implementation programs for agricultural extension, training, research, and seed production. It also finances studies on the diversification of agricultural production, marketing of livestock products, resource conservation, and agricultural credit. They are

expected to provide elements for extending the agricultural reform program in future phases of adjustment.

61. Social Dimensions of Adjustment. The financial rehabilitation program provides for an increase in current expenditures of development-oriented ministries and, thus, aims at improving basic public services in Chad. It also includes the formulation of sectoral strategies as a basis for rationalizing government expenditure programs in the medium term. While these elements of the adjustment program would improve social services, Chad still faces a decline in per capita income during the adjustment period. It therefore is desirable to introduce, in the short run, programs that aim at protecting the most vulnerable groups and at attenuating possible negative effects of the adjustment program. To this end, Chad is participating in the Social Dimensions of Adjustment Project. In addition to studies which would evaluate social welfare, an action program will be prepared to protect the most vulnerable groups. It will be developed in cooperation with other donors and will assess the possibility of relying on non-governmental organizations for its implementation. An IDA credit would be proposed later in FY90 to support this action program.

#### IV. THE PROPOSED OPERATION

##### A. History

62. The proposed Financial Rehabilitation Credit (FRC) would support the first phase of the Chadian Government's adjustment program. It would also provide fast-disbursing budget support to a Government which has experienced severe resource constraints due to political conflicts of recent years and to the serious decline in cotton revenues. The preparation of the credit builds on the Policy Framework Paper 1987-90 and on the 1987 Country Economic Memorandum. The content of the proposed credit was first discussed with the Government in an identification mission in July 1987, which was followed in October/November 1987 by a preparation/pre-appraisal mission; appraisal took place in February 1988. Negotiations were held in Washington in June 1988; the Chadian delegation was headed by H. E. Soumaïla Mahamat, Minister of Planning. Preparation of the program was facilitated by a UNDP-financed, Bank-executed technical assistance project to strengthen the capacity of the Ministry of Planning. Technical assistance to implement the program and prepare future phases of adjustment will, in addition to the UNDP-project, also be provided through the Economic and Financial Management Project. Supplementary data on the proposed credit and program are presented in Annex II.

##### B. Economic and Social Impact of the Adjustment Program

63. The adjustment program aims at strengthening the basis for future economic growth and, thus, reversing the declining trend in per capita income. Increasing efficiency of resource use in the public sector and in the cotton sector would allow the country to make better use of its existing investments and to orient expenditures under the program into productive uses. To achieve these objectives, substantial capital inflows, mainly in the public sector, are required to finance continued high current account and budget deficits. The anticipated impact of the adjustment program is presented in Table 3 and contrasted with a scenario without adjustment.

64. Public Finance. Under the adjustment program, reform of petroleum product taxation would permit a one-time increase in government revenues, of about 25%, from CFAF 18.2 billion in 1987 to CFAF 22.2 billion in 1988. Thereafter, implementation of reforms prescribed in the upcoming fiscal study should permit growth of tax revenues at a rate equaling or surpassing nominal GDP growth. Restructuring of the cotton sector may also make it possible to reintroduce cotton sector taxation during a later phase of adjustment, if cotton profitability increases.

65. The adjustment program provides for a higher level of government spending, including an increase in operating expenditures in key development ministries. Increased fiscal revenues combined with non-project aid would allow government current expenditures to rise to 8.6% of GDP in the 1988-90 period and 9.1% in 1991-95. This would, however, result in a widening budget deficit, reaching an average of 2.0% of GDP in the 1991-95 period. In the absence of an adjustment program, the much lower revenue level combined with a lack of external budget support would force the Government to severely curtail expenditures; while this would bring down the budget deficit, it would also limit government operations essential for growth and meeting the basic needs of the population.

66. Balance of Payments. Reforms in the cotton sector would allow cotton fiber exports to expand, thus boosting exports in constant prices by 6.2% per annum during 1988-90, decelerating to about 2.5% per annum in later years. Increased export earnings plus a high level of capital inflows would permit a higher level of imports. The current account deficit would decline modestly as a share of GDP while import growth is maintained. In contrast, without adjustment in the cotton sector, the expansion in cotton export volume would not be feasible since the operating losses of COTONTCHAD would increase with higher production levels. The resulting lower growth in export earnings combined with external funding constraints would, thus, limit import growth.

67. External Debt. The rapid increase in capital inflow during the adjustment period would increase external debt outstanding and disbursed from 23% of GDP at end-1987 to 42% of GDP at end-1995. The Government is committed to borrowing only on highly concessional terms, so that Chad's debt service ratio would remain a relatively low 9-16% throughout the 1988-95 period. Without adjustment, the debt service ratio would be lower, reflecting lower capital inflows.

Table 3: Selected Economic Indicators,  
With and Without Structural Adjustment  
(1987-1995)

|   | Actual<br>1987 | With<br>Adjustment<br>----- |         | Without<br>Adjustment<br>----- |         |
|---|----------------|-----------------------------|---------|--------------------------------|---------|
|   |                | period average<br>1988-90   | 1991-95 | period average<br>1988-90      | 1991-95 |
| GDP growth,<br>constant prices (%)                      | 0.5            | 2.6                         | 3.9     | 1.9                            | 2.5     |
| <u>As a share of GDP</u>                                |                |                             |         |                                |         |
| Total public investmmt <u>1/</u> 17.4                   |                | 19.0                        | 20.0    | 24.0                           | 23.0    |
| Public fixed investmmt <u>1/</u> 7.1                    |                | 8.0                         | 8.7     | 10.0                           | 10.0    |
| Government current<br>expenditures                      | 8.7            | 8.6                         | 9.1     | 8.1                            | 7.0     |
| Government current<br>budget deficit                    | -2.5           | -1.6                        | -2.0    | -1.5                           | -1.1    |
| External current<br>account deficit                     | -33.5          | -28.8                       | -22.1   | -19.0                          | -23.0   |
| External debt<br>(disb. at end<br>of period)            | 23.4           | 35.6                        | 42.1    | 26.6                           | 32.8    |
| Export growth (GNFS)<br>constant prices (%p.a.)         | 1.2            | 6.2                         | 2.5     | 1.5                            | 1.3     |
| Import growth (GNFS)<br>constant prices (%p.a.)         | 6.3            | 3.7                         | 3.0     | 0.7                            | 2.1     |
| Scheduled public debt<br>service/exports                | 6.5            | 13.6                        | 10.3    | 9.7                            | 7.6     |
| Scheduled public debt<br>service/government<br>revenues | 17.0           | 24.3                        | 22.7    | 21.1                           | 18.7    |

Source: Government data and Bank staff projections

1/ Total public investment comprises all foreign-funded projects included in the investment program; public fixed investment refers to fixed capital formation only.

68. Growth and Social Welfare. The adjustment program focuses on measures to improve the efficiency of the public sector and the cotton sector. Improvements in investment programming would, in the medium term, strengthen the basis for economic growth. The increase in cotton production under the program combined with a reduction of input cost would result in higher cash incomes in the principal agricultural zones of the country. Since the measures are being introduced gradually and their impact will be felt with some lags, the adjustment program is unlikely to result in an increase in real per capita income in the short term. It is expected that, starting in the early 1990s, the effect of the adjustment program, combined with the beginning of petroleum production, would increase economic growth to 3.9% p.a. which would reverse the current downward trend in per capita income. In the absence of an adjustment program, real per capita income growth would remain below the projected 2.6% population growth rate.

69. The adjustment program would have mainly positive distributional effects. In public finance, it would increase and rationalize current expenditures in the social sectors as well as the delivery of agricultural services. In addition, sectoral strategies are being prepared to further strengthen the provision of basic services to larger parts of the population. In the cotton sector too, the distributional impact of the adjustment program is expected on balance to be positive. As mentioned above, the Government is also addressing social development issues affecting particularly vulnerable groups through a social development project.

### C. Benefits and Risks

#### Benefits

70. Seen in the context of Chad's reconstruction efforts, there are three main benefits of the financial rehabilitation program. First, it would contribute to improvements in public finance, including increased resource mobilization, a focused public investment program, and an increase in current expenditures in development-oriented sectors. Second, it would result in a fundamental restructuring of the country's main export sector, cotton, and third, it would lead to an improved financial position of the public sector, especially through the settlement of arrears. The overall contribution of the program to the Chadian economy will be a strengthening of the foundations for higher growth in the 1990s. The adjustment program also provides a framework for aid-coordination and for obtaining higher levels of external assistance in the appropriate form and on very concessional terms.

#### Risks

71. The financial rehabilitation program is subject to considerable risk. As other operations in Chad, it would be adversely affected by external risks, such as drought and increased border conflicts which may divert public sector resources and delay the implementation of policy reform measures. There are also risks inherent to the financial rehabilitation program. First, the Chadian Government has to demonstrate its ability to implement and sustain the reform program. Second, it is possible that farmers will not increase their productivity to the extent anticipated under the program, thus diminishing the anticipated benefits. Efforts have been made in the design of the program to reduce these risks, through, e.g. a phased implementation of the reforms and technical assistance being provided to the Government for the preparation and implementation of the reform program.

### D. Proposed Financing

72. The proposed financing of US\$42 million for the FRC is composed of US\$16.2 million from IDA, US\$21.3 million from the Special Facility for Africa, and US\$4.5 million equivalent in joint parallel financing from the Saudi Fund. The IDA share was determined on the basis of IDA's lending program for Chad and in view of the country's other priority needs for which IDA assistance has been requested.

73. The proposed FRC would finance about 11% of Chad's merchandise imports in the period July 1988 through December 1989 and meet about 7%

of the country's gross external capital requirements for the same period. The counterpart funds of the credit are equivalent to 22% of Chad's current budget in these 18 months.

74. Significant cofinancing has been arranged for the financial rehabilitation program from the African Development Bank and the Government of France. The African Development Fund will contribute FUA30 million in cofinancing of the FRC. France is providing US\$26 million equivalent in budgetary assistance in 1988 and has announced that the Caisse Centrale will also make available a loan, on concessional terms, of US\$25 million equivalent to be disbursed during the three years of the program. Of this amount, US\$16 million equivalent could be disbursed in 1989. The 1988-89 financing plan includes substantial amounts of non-projects funding forthcoming from other donors as well. USAID is providing US\$7 million p.a., the European Community is providing about US\$11 million in STABEX funding for the cotton program in 1988, and the Netherlands is providing a total of about US\$12 million. There is, thus, considerable burden sharing among donors.

#### E. Disbursement, Procurement, Administration and Auditing

75. The proposed credit would be disbursed in two equal tranches. The first tranche would disburse entirely the SJF funds as well as US\$12.5 million equivalent of the SFA funds and US\$4 million equivalent of the IDA funds. The second tranche would consist of the remaining US\$8.8 million equivalent of SFA funds and US\$12.2 million equivalent of IDA funds. It would be disbursed following a tranche review in early 1989, six to nine months after Board presentation.

76. The credit would reimburse 100% of the foreign exchange costs of eligible imports on the basis of evidence that they were imported and paid for after credit signing. Due to Chad's acute funding shortage for the 1988 budget and to ensure that adequate funding is available to increase recurrent expenditures in the second half of 1988, retroactive financing of imports during the four months preceding the month of credit signing would also be permitted up to a maximum of 20% of the respective credit amounts. Eligibility for reimbursement from the African Facility Credit would be limited to imports from Part II members of IDA and from other countries designated as eligible by the Administrator under the African Facility. All arrangements for disbursement of the Saudi Fund contribution would be made in accordance with an Aide-Mémoire between IDA and the Saudi Fund for Development dated July 3, 1985. Expenditures for goods procured under invoices for US\$10,000 equivalent or less would not be eligible for financing out of credit proceeds. Both private and public sector imports would be eligible for financing. Imports by private entities would follow normal commercial practices. For public sector imports, procurement would be made through international competitive bidding for contracts of US\$1 million or more, while for lesser amounts the purchaser's normal procurement procedures which are acceptable to IDA, would apply.

77. To facilitate disbursement and procurement, two special accounts would be established at the Central Bank on behalf of the Treasury, one each for the IDA credit and the SFA credit. The Government of Chad would be the borrower. The regional Central Bank, BEAC, would be responsible for maintaining the credit accounts and supporting expenditures on the basis of eligible imports (negative list)

for submission to IDA. After effectiveness, initial deposits of US\$1.5 million each would be made by IDA and the SFA into the respective special accounts. These accounts would be replenished regularly and up to the limit of the First Tranche on the basis of fully documented reimbursement applications for amounts in excess of US\$1 million and on the basis of statements of expenditures under that amount. The minimum amount of replenishment applications would be US\$300,000. The Central Bank would indicate on the statements of expenditures the nature and origin of the goods, as well as the payment date, and would maintain all relevant supporting documentation (invoices, import certificates and evidence of payment) for review by supervision missions. Expenditures covered by the IDA credit would be in accordance with normal IDA rules while expenditures covered by the SFA credit would be in accordance with the resolution establishing the SFA.

78. Within six months after the completion of disbursements, an external audit report, conforming to internationally accepted standards prepared by Bank approved auditors, would be submitted to IDA.

#### **F. Monitoring and Tranche Release**

79. Responsibility for monitoring the implementation and impact of the structural adjustment program would be with the Interministerial Committee that the Government has set up for this purpose, under the chairmanship of the Ministry of Planning. It would evaluate the need for additional adjustment measures and work closely with the Bank, the African Development Bank, the IMF and other donors in reviewing progress in implementing the adjustment program.

80. Release of the second tranche of the credit would be preceded by a review, by IDA and the co-financiers, of progress in the implementation of the adjustment program. Tranche release would be based on a review of general progress in implementing the program and, in particular, on the following measures having been taken: (i) implementation of the supplementary budget for 1988; (ii) adoption of the three-year rolling investment program for 1989-91; (iii) adoption of the 1989 current budget including an increase in non-personnel operating expenditures of development-oriented ministries; (iv) satisfactory completion of the review of COTONTCHAD's performance in reducing costs, and a decision on lowering the floor price for the 1989/90 cotton crop year; (v) establishment of a Fund to support the cotton producer floor price and a mechanism for distributing the cotton sector surplus; and (vi) significant progress in the public enterprise studies. The African Development Bank has indicated that it would apply the same tranching conditionality as IDA.

81. The Interministerial Committee would submit to IDA a progress report on the adjustment program in time for the tranche review. This report would serve as a basis for the continuing dialogue with IDA and the other donors. The Government of Chad would submit to IDA a final report on the implementation of the financial rehabilitation program upon full disbursement of the credit.

#### **V. BANK OPERATIONS STRATEGY**

82. Twenty IDA credits totalling US\$144.2 million equivalent have been approved for Chad as of March 31, 1988. Twelve of these credits

(US\$43.6 million equivalent) have been fully disbursed, and two (US\$19.1 million equivalent) were cancelled before becoming effective because of the 1979-82 war. All Bank Group operations in Chad were suspended in July 1979 because of accumulated arrears on IDA credits, although escalating hostilities had already halted project activities and led to considerable damage to project assets. The Bank resumed its activities in Chad in mid-1985 and four operations (US\$65.2 million equivalent) have been approved as of March 31, 1988. Of the 18 credits (excluding the cancelled ones), nine were for agricultural or rural development, five for education, three for highways, and one for economic and financial management. In addition, credits for a Road Reconstruction Project and a National Livestock Project were approved by the Board in April and May 1988 respectively. Annex I contains a summary Statement of Bank Group Operations in Chad.

83. IDA's assistance strategy for Chad supports the Government's strategy outlined in its Interim Development Plan 1986-88 and its adjustment program described above. The strategy is more fully described in the Country Brief distributed to the Executive Directors in May 1988. The strategy supports investments in the productive sectors (agriculture, livestock, and energy) as well as transport infrastructure, and begins to emphasize development of human resources. IDA also aims at strengthening economic management, begins to support macro-economic policy reform, and places increased emphasis on aid coordination. This strategy supports urgently needed reconstruction and rehabilitation works, and moves progressively towards macro-economic and sectoral reforms.

84. The Bank's strategy for the agricultural sector is shifting from emergency assistance through the Emergency Cotton Sector Program in FY86 (Credit No. 1716) and the Agricultural Rehabilitation Project (Credit No. 1775) in FY87 to subsector operations supporting investments and policy reforms. A National Livestock Development Credit, approved by the Executive Directors in May 1988, would support the Government's efforts to increase livestock production, improve livestock health, and reform marketing. Additional sector work is underway to help define the objectives and content of the Bank's future agricultural lending in Chad. An agricultural services project (FY91) to strengthen extension and research is being prepared. An agricultural sector adjustment credit (FY92S) would support policy reforms in the following areas: (i) the cotton sector, by pursuing the adjustment measures supported under the proposed Financial Rehabilitation Credit; (ii) the irrigation sector, by implementing a cost effective strategy for the development of irrigated agriculture; and (iii) food security.

85. In transport, the Bank supports the Government's strategy which is presented in a sector strategy paper and a six-year investment program, both prepared with IDA assistance. They were presented to the donor community in February 1988. The strategy focuses on completing the rehabilitation and maintenance of the high priority road network, strengthening the planning and management capacity of sector institutions, improving road maintenance financing and air transport services, and promoting private participation in the sector. The Road Reconstruction Credit (Credit No. 1728) would complete the rehabilitation of high priority roads. A Transport Sector Project (FY90) would assist with the implementation of the policy and institutional elements of Chad's sector strategy including strengthening

of sectoral planning and management, private sector development, and ensuring adequate financing for maintenance.

86. In the energy sector, the Bank would support the Government's efforts to reduce its dependence on petroleum imports. A petroleum project (FY91) would include well development, a pipeline, a micro refinery, and modifications to the power stations in N'Djamena and other major cities. A technical assistance project (FY91) would strengthen the Ministry of Mines and Energy in petroleum matters and assist with the promotion of petroleum exploration.

87. In human resources, the Government has begun the reconstruction of the country's social infrastructure dismantled by the recent period of war. In the education sector, the Bank will participate in the reconstruction effort first through an Education Rehabilitation Project (FY89). It will concentrate on primary schools, providing assistance to low-cost community-based construction and learning materials, and on teacher training and institutional strengthening. In the health sector, the Bank also envisages assisting in the rehabilitation of the basic health care system and the management capabilities of the Ministry, based on a sector survey scheduled for FY89. Policy options for addressing the most pressing human resources issues will be identified in a series of studies and discussed at a Round Table on education, scheduled for 1989. Further analytical work is planned through a manpower assessment survey in 1990.

88. In addition to institution-building efforts included in investment operations, IDA is providing assistance to ministries concerned with macro-economic management through free-standing technical assistance projects. IDA is the implementing agency for a UNDP-financed Technical Assistance Project that is providing a team of experts to the Ministry of Planning. An Economic and Financial Management Project, approved by the Executive Directors in January 1988, will complement the UNDP project. It includes studies to prepare policy reforms in the areas of public enterprises, public administration, and fiscal policy. The project also finances a demographic survey.

89. IDA expects to continue adjustment lending to Chad through structural and sectoral adjustment operations. A follow-up adjustment operation in 18-24 months is expected to deepen the adjustment effort, especially in public finance, and to extend it to the parastatal sector. The sector operations mentioned above for agriculture, transport, and education will also support sectoral policy reforms. A Social Development Program (FY90) is under preparation to address the social impact of adjustment and explore new approaches to social development.

## VI. COLLABORATION WITH THE IMF

90. Since 1985, when the Bank resumed lending operations in Chad, the Bank and the Fund have closely coordinated their activities and assisted the Government with the preparation of the Policy Framework Paper for 1987-90. A first-year SFA program, approved on October 30, 1987, is currently underway in Chad. IMF staff worked with the FRC preappraisal and appraisal missions, and cooperation on the adjustment program continues. In particular, Bank and Fund staff worked closely in the area of petroleum taxation, and the Government has requested Fund assistance for the upcoming fiscal study.

**VII. RECOMMENDATIONS**

91. 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.

92. I am satisfied that the proposed African Facility Credit would comply with the provision of Resolution No. IDA 85-1 of May 21, 1985, and recommend that the Executive Directors approve the proposed African Facility Credit.

**Barber B. Conable  
President**

**Attachments  
Washington, D.C.  
July 5, 1988**

CHAD: Key Macroeconomic Indicators 1/  
(percent, except where indicated)

|  | 1983  | 1984  | 1985   | 1986   | 1987   | 1988   | 1989   | 1990   | projected |        | 1993   | 1994   | 1995   |
|--|-------|-------|--------|--------|--------|--------|--------|--------|-----------|--------|--------|--------|--------|
| Gross Domestic Product growth rate     | 5.6   | -5.8  | 29.0   | -2.3   | 0.5    | 3.1    | 2.3    | 2.4    | 2.4       | 2.4    | 8.0    | 3.3    | 3.3    |
| Gross Domestic Income growth rate      | 9.4   | -5.2  | 28.3   | -2.5   | 0.5    | 3.4    | 2.0    | 3.4    | 3.0       | 3.0    | 8.5    | 4.2    | 4.0    |
| GDI per capita growth rate             | 6.9   | -7.7  | 25.1   | -5.1   | -2.1   | 0.8    | -0.6   | 0.0    | 0.4       | 0.4    | 5.0    | 4.2    | 4.0    |
| Consumption per capita growth rate     | 8.0   | -5.1  | 16.1   | -10.0  | -3.5   | -0.7   | -0.7   | -0.8   | 0.0       | 0.7    | 3.1    | 0.3    | 1.5    |
| Debt Service (US\$ million) 2/         | 0.0   | 6.4   | 9.0    | 10.0   | 10.9   | 23.5   | 33.5   | 30.3   | 30.5      | 30.9   | 25.0   | 29.1   | 29.5   |
| Debt Service Ratio 3/                  | 0.0   | 3.9   | 7.3    | 7.2    | 6.5    | 12.0   | 15.9   | 13.0   | 12.2      | 11.7   | 9.2    | 9.2    | 0.0    |
| Debt Service as % of GDP               | 0.1   | 1.2   | 1.4    | 1.2    | 1.1    | 2.0    | 2.6    | 2.2    | 2.1       | 1.9    | 1.4    | 1.5    | 1.4    |
| Gross Investment/GDP                   | 5.0   | 7.1   | 9.0    | 17.2   | 18.4   | 18.4   | 19.0   | 19.5   | 20.0      | 20.0   | 20.0   | 20.0   | 20.0   |
| Domestic Savings/GDP                   | -2.2  | -1.4  | ..     | ..     | -12.4  | -11.5  | -11.5  | -9.9   | -9.5      | -9.8   | -6.7   | -5.3   | -5.3   |
| National Savings/GDP                   | -3.7  | -2.8  | ..     | ..     | -15.1  | -14.0  | -14.5  | -12.5  | -11.0     | -11.9  | -9.2   | -6.7   | -6.5   |
| Marginal National Savings Rate         | ..    | ..    | ..     | ..     | ..     | 0.0    | -0.1   | 0.5    | 0.1       | -0.1   | 0.3    | 0.3    | 0.0    |
| Public Investment/GDP                  | 4.0   | 6.1   | 0.0    | 10.2   | 17.4   | 17.4   | 18.0   | 18.5   | 19.0      | 19.0   | 19.0   | 19.0   | 19.0   |
| Public Savings/GDP                     | ..    | ..    | ..     | ..     | ..     | ..     | ..     | ..     | ..        | ..     | ..     | ..     | ..     |
| Private Investment/GDP                 | 1.0   | 1.0   | 1.0    | 1.0    | 1.0    | 1.0    | 1.0    | 1.0    | 1.0       | 1.0    | 1.0    | 1.0    | 1.0    |
| Private Savings/GDP                    | ..    | ..    | ..     | ..     | ..     | ..     | ..     | ..     | ..        | ..     | ..     | ..     | ..     |
| Public/Private Investment Ratio        | 4.0   | 6.1   | 0.0    | 10.2   | 17.4   | 17.4   | 18.0   | 18.5   | 19.0      | 19.0   | 19.0   | 19.0   | 19.0   |
| Government Budget Revenue/GDP          | 4.3   | 8.2   | 7.5    | 5.9    | 6.2    | 7.0    | 7.1    | 7.1    | 7.1       | 7.1    | 7.1    | 7.1    | 7.1    |
| Government Current Expenditure/GDP     | 6.6   | 10.3  | 9.1    | 8.6    | 8.7    | 8.6    | 8.6    | 8.7    | 9.1       | 9.1    | 9.3    | 9.2    | 9.0    |
| Budget Deficit/GDP                     | -2.3  | -2.1  | -1.6   | -2.7   | -2.5   | -1.6   | -1.5   | -1.6   | -2.0      | -2.0   | -2.1   | -2.0   | -1.9   |
| Export Growth Rate 4/                  |       | 21.2  | -25.9  | 15.4   | 16.0   | 16.8   | 7.1    | 9.9    | 7.1       | 5.6    | 5.0    | 12.9   | 0.2    |
| Exports/GDP                            | 23.6  | 32.4  | 18.5   | 17.3   | 17.0   | 17.7   | 18.2   | 18.9   | 18.9      | 18.6   | 17.4   | 18.1   | 17.7   |
| Import Growth Rate 4/                  |       | 10.8  | 53.5   | 9.5    | 22.0   | 16.3   | 7.9    | 1.8    | 5.5       | 5.2    | 1.1    | 4.9    | 5.3    |
| Imports/GDP                            | 35.1  | 44.1  | 52.2   | 46.3   | 47.8   | 47.9   | 49.6   | 49.2   | 49.9      | 50.5   | 46.7   | 47.0   | 47.4   |
| Current Account Balance (US\$ million) |       |       |        |        |        |        |        |        |           |        |        |        |        |
| Including official transfers.          | 14.0  | 8.0   | -89.0  | -53.0  | -84.8  | -77.5  | -101.3 | -82.1  | -89.2     | -100.2 | -81.1  | -70.2  | -79.0  |
| Excluding official transfers.          | -80.0 | -71.0 | -223.0 | -254.0 | -320.8 | -355.5 | -384.9 | -371.3 | -384.2    | -401.1 | -380.0 | -393.2 | -390.3 |
| Current Account Balance/GDP 5/         | -13.8 | -13.8 | -33.5  | -31.0  | -33.5  | -29.7  | -29.9  | -26.8  | -25.8     | -25.0  | -21.4  | -19.5  | -18.7  |

- 1/ All figures are percentages, unless otherwise specified; (..) indicates that the data compatible with the rest of the series is not available.  
 2/ Includes the interests on, and the repayments of arrears (\$77.4 million at the end of 1987).  
 3/ Debt service as a percentage of all exported goods and services.  
 4/ Based on current US\$ figures, including goods and non-factor services.  
 5/ Excludes public transfers and official capital grants.



THE STATUS OF BANK GROUP OPERATIONS IN CHAD

A. STATEMENT OF IDA CREDITS  
(As of May 31, 1988 )

Amount in US\$ million  
(less cancellations) a/

| <u>Credit No.</u>   | <u>Fiscal Year</u> | <u>Purpose</u>                            | <u>IDA c/</u> | <u>Undisbursed</u> |
|---|--------------------|---|---------------|--------------------|
| 2 credits have been cancelled and fully repaid b/<br>12 credits have been fully disbursed |                    |   | 43.59         |                    |
| Cr.489-1  | 1976               | Sategui-Deressia<br>Irrigation Supplement | 8.00          | 0.05               |
| Cr.811  | 1987               | Third Education                           | 8.30          | 3.03               |
| Cr.1716   | 1986               | Cotton Program                            | 15.00         | 7.48               |
| Cr.1728   | 1986               | Highway Maintenance                       | 20.00         | 15.16              |
| Cr.1775   | 1987               | Agriculture Sector<br>Rehabilitation      | 17.40         | 16.73              |
| Cr.1872   | 1988               | Economic and Financial<br>Management d/   | 12.80         | 13.65              |
| Cr.1901   | 1988               | Road Reconstruction d/                    | 47.00         | 46.95              |
|   | 1988               | Livestock d/                              | <u>18.60</u>  | <u>18.02</u>       |
| TOTAL   |                    |   | 190.69        | 121.07             |
| of which has been repaid  |                    |   | <u>1.98</u>   |                    |
| Total now held by IDA   |                    |   | <u>188.71</u> |                    |

Amount sold 5.08  
of which repaid 5.08

Total undisbursed 121.07

a/ Prior to exchange adjustments.

b/ The Second Livestock (US\$11.5 million) and Third Highway (US\$7.6 million) Projects were cancelled before becoming effective, on October 16, 1980. Supplemental credits were approved for the First and Second Education Projects and for the Sategui-Deressia Project.

c/ Credit No. 1716-CD and higher are denominated in SDRs and are shown in US\$ equivalent based on exchange rates in effect at the time of negotiations.

d/ Not yet effective.

B. STATEMENT OF IFC INVESTMENTS

Chad is not a member of IFC.

CHAD

FINANCIAL REHABILITATION CREDIT

Supplementary Program Data Sheet

Section I: Timetable for Key Events

- (a) Time taken to prepare program: 6 months
- (b) Departure of Appraisal mission: February 5, 1988
- (c) Completion of Negotiations: June 20, 1988
- (d) Planned Date of Effectiveness: October 30, 1988

Section II: Special Bank Implementation Actions

None

Section III: Special Conditions

- (a) Conditions for Credit Effectiveness
  - (i) Adoption of supplementary budget for 1988 reflecting increase in non-personnel operating expenditures of development-oriented ministries;
  - (ii) Execution of COTONTCHAD's "contrat-plan"
- (b) Conditions for Release of Second Tranche
  - (i) General progress in implementing the financial rehabilitation program;
  - (ii) Implementation of the supplementary budget for 1988;
  - (iii) Adoption of the investment program for 1989-91;
  - (iv) Adoption of the 1989 current budget, including an increase in non-personnel operating expenditures of development-oriented ministries;
  - (v) Satisfactory completion of the review of COTONTCHAD's performance in reducing costs and a decision on lowering the floor price for the 1989/90 crop year;
  - (vi) Establishment of a Fund to support the cotton producer floor price and a mechanism for distributing the cotton sector surplus;
  - (vii) Significant progress in the public enterprise studies.

N'Djamena, June 20, 1988

Mr. Barber B. Conable  
President  
World Bank  
Washington, D.C.

Mr. Babacar N'Diaye  
President  
African Development Bank  
Abidjan.

Gentlemen:

I am pleased to send you this statement of development policy, which builds on the Policy Framework Paper for 1987-90, adopted in 1987. The Statement describes the first phase of the adjustment program being undertaken by the Government of Chad, and contains a request from the Government to the World Bank and the African Development Fund for a Financial Rehabilitation Credit (FRC) to support this first phase. I would therefore like to restate briefly the objectives of our adjustment program and the reforms already undertaken, and to describe the remaining actions that the Government intends to take during this first phase of adjustment of the Chadian economy.

Yours faithfully,

The Minister of Planning and  
Cooperation

GOVERNMENT OF CHAD

Statement of Development Policy

1. Recent Changes in Chad's Economy. Chad has experienced serious economic and financial difficulties over the past 20 years; per capita income (US\$150 in 1986) is one of the lowest in the world. These difficulties are largely attributable to Chad's low level of development and to the impact of successive droughts, factors that were aggravated by a long conflict of external origin which absorbed a significant proportion of Chad's already limited resources. Since 1983, however, Chad has made considerable progress toward political stability and economic reconstruction. Real GDP, which had fallen almost 20%, increased by 3% per year on average from 1983 to 1987 as a result of record cotton production in 1983/84 and the recovery in the agriculture and livestock sectors following the drought. Nevertheless, economic growth in 1986 and 1987 remained below the 2.4 % population growth rate, due to the cotton crisis, which adversely affected government revenues, exports, and rural incomes. In the face of this new crisis, the Government of Chad took urgent action to improve the performance of the cotton sector and austerity measures to reduce the budget deficit.
  
2. Development Plan. At the same time, the Government took steps to tackle Chad's fundamental development problems and the structural constraints in the economy. It defined the main lines of its development strategy in an Interim Development Plan 1986-88, which outlines major objectives and specific project proposals and was presented to the Round Table Donors' Conference in Geneva in December 1985. The Government's long-term development objectives are to ensure food self-sufficiency, diversify the base of the economy by reducing its dependence on cotton, restore and maintain the transportation network and accelerate the development of human resources. Work is in progress to establish the strategies and measures needed to achieve these objectives in priority sectors and at the macro-economic level.
  
3. Policy Framework Paper 1987-90. It is against this background that the Government, in conjunction with the World Bank and International Monetary Fund, prepared a Policy Framework Paper (PFP) for the period 1987-90. The PFP outlines the principal structural problems in the Chadian economy including: over-dependence on the cotton sector, the low level of physical, human and institutional infrastructure, the imbalances in public finances, inadequate performance by the public enterprises and constraints on credit to the economy. The main quantitative targets for the 1987-90 adjustment program are to: achieve an average annual economic growth rate of 2% in real terms, keep the rate of inflation to 5% a year, reduce the current account deficit (including official transfers) from 13.5% of GDP in 1985/86 to 10%, and contain the overall balance of payments deficit at an average of SDR 6 million (or about 25% of the average deficit for 1985 and 1986). The policy document contains a series of measures to be taken to achieve these targets. We have already received support from the International

Monetary Fund for the first year of this program in the form of an agreement under the Structural Adjustment Facility, reached in October 1987, and a first loan tranche for the period 1987/88. We intend to pursue this program.

#### Adjustment Program 1988-1989

4. On the basis of the PFP, the Government of Chad has drawn up a detailed reform program for 1988-1989. The aim during this phase of the adjustment program is to prepare the ground for reform of two sectors that are crucial for improving the utilization of economic resources: public finances and the cotton sector. These are also the sectors that require immediate and substantial financial support to maintain and strengthen their development. We have also embarked on a number of studies covering the public enterprise sector, public administration, and the social dimensions of adjustment, the results of which will serve to prepare later phases of the adjustment process. The Government of Chad has therefore initiated a process of economic policy reform which will be pursued in several stages and is designed to improve the effectiveness of our economic management and strengthen the base for Chad's long-term development. The 1988/1989 Action Plan appears in Attachment 1 of this letter.

#### A. Public Sector Resource Management

5. The 1988-1989 phase of the public resource management component covers the following five areas: sectoral strategies, the public investment program, current expenditures, fiscal reform and the public sector financing plan.

6. The Government intends to achieve the objectives outlined in the Interim Development Plan by implementing strategies prepared for the main sectors of the economy. These strategies will comprise analyses of sectoral problems, the identification of objectives and priorities, the development of sectoral criteria for selecting investments, a medium-term investment program, and analysis of the implications for the structure and volume of current expenditure, and cost recovery measures. The institutional aspects and the need to strengthen the administrative structure will also be addressed in these strategies. In conjunction with the World Bank, a strategy document for the transportation sector has already been prepared and was submitted to a donors' meeting held in N'Djamena in February 1988. Formulation of a development strategy for the rural sector and the irrigation subsector is underway. We intend to prepare strategies for the education and health sectors before the end of 1988 and 1989 respectively. Given the importance of external assistance for our development programs in each of these sectors, we plan to present these strategies to the donors. Moreover, preparation of a planning document began in May 1988. This exercise will allow us to analyze Chad's economic and social situation, to determine the country's strengths and weaknesses, to define sectoral strategies and to prepare action programs. The sectors for which development strategies have not been formulated will therefore be included in this exercise.

7. To ensure effective utilization of financing, the Government resumed the preparation of a public investment program in 1987 after an interval of 12 years. This effort has been intensified for preparation of the 1988 investment program. The program, amounting to CFAF 81 billion, emphasizes the development of the agriculture sector and the

rehabilitation and maintenance of the road network, and also launches a rebuilding of the social sectors. To improve the quality of the investment program we are undertaking additional studies, in the areas of irrigation, public enterprises and education; the conclusions of these studies will be incorporated into the final decisions on project implementation. The Government intends to introduce a three-year rolling public investment program. With this purpose, we prepared a public investment program for the years 1988-90 in December 1987. This program will be updated annually and reviewed with the World Bank and other interested donors. This program will be updated annually. We are well aware of the problem of recurrent charges arising from investments. Some 60% of the assistance provided by donors is being used to meet Government operating expenditures and the costs of training and technical assistance relating to investment projects. Given the present low debt servicing potential of Chad's economy, we are continuing to seek external financing in the form of grants and loans on highly concessional terms. We are in the process of strengthening the preparation and monitoring of the investment program with the support of UNDP and the World Bank. In April 1988, selection criteria for public investments were adopted by the Ministry of Planning and Cooperation. Finally, as regards the social sectors, we are studying ways of maximizing use of available resources by encouraging the financial participation of beneficiaries.

8. The adjustment program also includes an augmentation and restructuring of current expenditures under the support of the Financial Rehabilitation Credit (FRC). The restructuring is aimed at increasing the real operating expenditures of key development ministries whose budget allocations have been shrinking in recent years as a result of severe financial constraints. The current level of real expenditures in these ministries is inadequate to carry out even the most basic operations and leads to the inefficient use of our resources. From mid-1988 onward, the Government will increase real operating expenditures in the following ministries: Agriculture; Livestock and Rural Water Supply; Public Works, Housing and Urbanism; Transport and Civil Aviation; Education; Public Health; Social Affairs and the Advancement of Women; and Tourism and Environmental Protection. For 1988 total expenditure by these ministries will be CFAF 2 billion. Part of the necessary resources will come from budget assistance on terms equivalent to those of IDA, in the amount of CFAF 1,500 million. The remaining resources will come from the budget as agreed with the IMF. To the extent necessary, budget allocations as a whole will be adjusted through supplementary allocations to be introduced in July 1988. The new allocations will be implemented as fully as circumstances permit so that actual and planned expenditures coincide as closely as possible. The overall increase in current expenditures and in the current deficit in relation to the totals agreed with the IMF under the structural adjustment facility will not exceed the additional amount provided for in the Financial Rehabilitation Program. We are in the process of strengthening the procedures for preparing, executing and monitoring operating expenditures within the Ministry of Finance and Technology and the Ministry to the Presidency in charge of General Inspection and State Control. The Government is currently taking measures to streamline expenditure authorization procedures (described in Attachment 2) so as to render the system more efficient without impairing necessary Government control. In 1989, we will ensure that the growth of real expenditures in the ministries mentioned above is in line with the growth of government revenues and with budget policy objectives to be

agreed with the IMF, the World Bank, the African Development Bank, and France.

9. The Government is concerned with the current status of the civil service and recognizes the need for reform. With the support of USAID, we have already embarked on a census of civil servants. As part of the first phase of adjustment, a study of the civil service/administration will be conducted in order better to identify the personnel needs of the various departments and the qualifications required, and to compare these with current numbers. The Chadian Government has already undertaken a similar study in the Ministry of Education with French assistance. The results of these studies and the projections for government revenues will be factored into any reform of the civil service. As well, civil service reform must deal with the question of the remuneration of civil servants, who for the most part are receiving only 60% of their 1967 salary base. Reforms resulting from these studies will be undertaken during the second phase of the program. The Government is currently taking measures to pay the salary arrears of National Education personnel as determined on July 1, 1988; no new arrears will be allowed to accumulate with respect to this group.

10. Given the gradual normalization of payroll and operating costs, as well as the increase in recurrent costs associated with new investments, the Government is aware of the need to raise consolidated budget revenue in relation to GDP. In 1988, revenue growth will depend largely on the results of the new system of taxing petroleum products that came into effect in August 1987. Initial difficulties encountered in implementing the new system are being overcome: since November, various steps have been taken to improve the way it is administered and to speed up the collection process. Measures will also be introduced in 1988 to expand the taxation of oil importing companies and limit their exemptions. On the basis of current import duty assessments, we are already able to set our budget revenue target in this area at CFAF 4.5 billion for 1988. However, a sustainable increase in budget revenue cannot depend solely on the taxation of petroleum products. Other, supplementary sources of revenue will be tapped as far as allowed by the degree of overall fiscal pressure the economy can sustain. To this end, a general study of the whole field of taxation will be undertaken in conjunction with the International Monetary Fund and the World Bank. On the basis of this study and other pertinent data, new taxation measures will be introduced to the extent possible with the 1989 budget.

11. The Government confirmed its intention to respect the financial program established with the staff of the International Monetary Fund for 1988. This program sets out the objectives mentioned above for taxation of petroleum products, overall revenues and expenditures, as well as the consolidated budget deficit presented in Attachment 3 of this statement of development policy. Implementation of the 1988 budget will be examined in collaboration with the staffs of the International Monetary Fund and the World Bank.

12. The public sector financing plan (Attachment 3), covering both the general budget and the cotton sector, takes the form of a summarized statement of our goals for 1988 and 1989. It incorporates current expenditures, revenues and capital investment, and provides an estimate of our overall financing needs, including those relating to the settlement of COTONTCHAD's arrears. Although the figures on external financing for 1989 should be taken as indicative, it is apparent --

given the order of magnitude of the country's external financing requirements -- that significant and sustained non-project support will be needed. Moreover, the constraint represented by possible settlement of the arrears of COTONTCHAD will allow no progress toward an effective solution unless agreement can be reached with the Central Bank on lowering the charges that now apply. The Government is determined to set up a plan, designed in conjunction with donors, for settling these arrears within a reasonable period, and to see to it that the plan is carried out.

## **B. Cotton Sector**

13. The Government introduced an emergency program in 1986 to respond to the crisis in the cotton sector. The crisis was precipitated by the sharp fall in the world price of cotton in 1985, and coincided with a period of lax financial management in COTONTCHAD which resulted in accumulated operating losses of CFAF 41 billion. With the support of the World Bank and other donors, the Government undertook an emergency program covering the 1986/87 and 1987/88 agricultural seasons. The emergency program has succeeded in cutting COTONTCHAD's costs by around 40% and reducing its operating losses from CFAF 23 billion in 1985/86 to CFAF 5 billion in 1987/88.

14. After this initial phase, the Government began to implement a program of basic reforms covering the period 1988/89-1990/91 to re-establish the medium-term economic and financial viability of the cotton sector. This program has four components:

- (a) a program to increase the efficiency of COTONTCHAD. A number of measures have been identified to improve the efficiency of COTONTCHAD. In order to reduce administrative costs and improve management, most services and personnel will be transferred from the N'Djamena headquarters to the production site (Moundou) by May 1989. This will be accompanied by the following actions: revision of the organizational chart, clarification of the division of responsibilities among the top managers, as well as a management support and training program;
- (b) a program which aims to improve cotton production which includes support to extension and research services. This component aims to:
  - increase cotton production;
  - raise farmers' productivity;
  - reorient the work programs of the extension (ONDR) and research (IRCT) agencies to respond to farmers' needs;
  - strengthen coordination between COTONTCHAD, ONDR and IRCT; and
  - allocate funds for IRCT and ONDR's expenditures in the government's budget to the extent possible given available resources.

- (c) the establishment of a flexible producer pricing system and a new price support mechanism. The Government has adopted a more flexible producer pricing policy designed to take into account fluctuations in world cotton prices and to reduce and eventually eliminate the sector's deficit. To this end, the Government has introduced a price differential for three qualities of seed cotton and will reduce the floor producer price to a maximum of 90 CFAF per kilogramme for first quality seed cotton for the 1989/90 and 1990/91 seasons. By November 1988, the Government will also establish a fund to support the floor producer price and develop guidelines for allocating surpluses that arise from high world prices; such guidelines will give top priority to farmers.
- (d) a plan for settlement of COTONTCHAD's arrears. In order to reduce COTONTCHAD's arrears to the banking system, the Government has begun discussions with the Central Bank which appears to be favorably disposed to the idea of freezing the arrears falling under the 1984 moratorium, for a period which has not yet been determined. Negotiations are underway with other donors to settle the balance of the arrears.

15. A contrat-plan, which is to be adopted by August 1988, defines the environment within which the objectives of the restructuring program will be achieved, the means for achieving these objectives, the schedule for the program's execution, as well as the Government's and COTONTCHAD's respective commitments under the program.

### C. Preparation of Future Reforms

16. As indicated above, this first phase of our adjustment program includes studies to prepare for reforms that will be undertaken during later stages of the program. We have already referred to studies of the tax system and the civil service, which will provide a basis for further reforms in the area of public finances. We also envisage studies on public enterprises, the agriculture sector, education and training, and the social dimensions of adjustment.

17. We are preparing a reform program to improve the performance of public enterprises and to rationalize the economic environment in which they operate. We have already initiated a first batch of five diagnostic studies of public enterprises, which will be completed before the end of 1988; we intend to begin studies on a second batch of enterprises by the end of 1988. A study of cross arrears among parastatals is also underway. The restructuring of the cotton sector described above is an important part of this reform. We have also taken measures in two other sectors: in livestock, we have decided to deregulate the distribution of veterinary products in mid-1988 and their importation as of January 1, 1991; we have also decided to eliminate export restrictions on livestock and to rationalize administrative procedures in April 1988. A complete system of cost recovery for veterinary services was introduced in April 1988. In the transportation sector we initiated a study in November 1987 of the functions of the CTT (Coopération des Transporteurs Tchadiens) and a study of the possibility of privatizing quarrying operations currently undertaken by OFCA.

18. In the area of rural development, we plan to conduct two major studies. The first we envisage as a master plan for development of the Sudanese zone, where the principal income-producing activity until now has been cotton-growing. While taking current development programs and existing studies into account, it will incorporate all possible avenues of development (diversification of output, upgrading and/or building of roads, storage facilities, reorganization of extension services, intensification of research, means of transportation, marketing organization, processing of products, transportation of products to deficit areas, etc.), the final goal is a well-balanced development of this zone and its integration with the rest of the country. The second major study proposed, which will prepare the way for reforms in the agricultural sector, is concerned with the problem of food security.

19. As regards the education/training sector, over the next two years we intend, on the basis of studies supported in IDA, ADB and the French Government, to prepare a sectoral policy framework that will enable us to avoid major structural distortions in this important sector and to achieve balanced development of the different levels of education in innovative ways, while taking into account priority training needs, our budgetary constraints and changes in our employment market.

20. With regard to the social dimensions of the adjustment program, we have begun the work of collecting statistics on population and living standards; we have also begun to prepare complementary measures. In particular, we will take account of the social dimensions of adjustment in formulating strategies for the social sectors and in the allocation of current expenditures. We envisage a sociological study, a medium-term demographic study and a mini-survey of incomes and consumption. We also hope to study the potential impact of reductions in the civil service and in the staff of public enterprises before implementing reforms in these areas. We intend, with donor assistance, to create a fund to provide support and start-up help to new small holders in marginal cotton-growing areas and COTONTCHAD personnel dismissed as a result of measures taken as part of the emergency program and the adjustment program. This Fund will also support projects and programs in urban and rural small-scale enterprises, the improvement of urban and rural living conditions, as well as nutrition and health.

Attachment 1: Action Plan

Attachment 2: Budgetary Procedures

Attachment 3: Public Sector Financing Plan, 1988-89

Attachment 1

CHAD - FINANCIAL REHABILITATION PROGRAM 1988 - 1989

ACTION PLAN

| <u>Measure</u>   | <u>Completion Date</u>  |
|--|---|
| <b>I. <u>Public Sector Resource Management</u></b>   |   |
| <b>1. <u>Public Investment Program (PIP)</u></b>   |   |
| a. Adopt 1988 PIP  | January 1988  |
| b. Prepare studies on specific projects<br>- Sugar<br>- Irrigation   | March 1988  |
| c. Adopt first rolling PIP for 1989-91   | January 1989  |
| d. Strengthen investment program preparation<br>and evaluation process   | June 1988   |
| e. Formulate sectoral strategies<br>- Livestock<br>- Transport<br>- Education<br>- Health  | 1988-1989<br>March 1988<br>January 1988<br>end 1988<br>end 1989 |
| f. Hold sectoral aid coordination meetings<br>- Agriculture<br>- Transport<br>- Education  | December 1986<br>February 1988<br>mid-1989                      |
| <b>2. <u>Operating Budget</u></b>  |   |
| a. Increase through supplementary financing<br>non-personnel operating expenditures for<br>second semester 1988 in eight development<br>ministries | July 1988   |
| b. Adopt 1989 budget, including increased<br>non-personnel operating expenditures for<br>the eight ministries                                      | December 1988   |
| c. Strengthen expenditure authorization<br>and monitoring procedures   | February 1988   |

**3. Fiscal Policy**

- a. Replace differentiated petroleum import tax system with unitary consumption tax July 1987
- b. Reinforce recovery efforts of petroleum tax November 1987
- c. Prepare an overall study of the fiscal system, including special funds Before end 1988

**II. Restructuring of the Cotton Sector**

**1. Restructuring of COTONTCHAD**

- a. Transfer COTONTCHAD's financial and administrative services to Moundou May 1989
- b. Adopt a new organizational plan and redefinition of responsibilities October 1988
- c. Create an agricultural input management office July 1988
- d. Adopt a training program January 1989
- e. Adopt a supplemental program to improve performance of DHS November 1988
- f. Define a commercial policy for DHS March 1989
- g. Negotiate with CTT a reduction of transport prices for 1989/80 agricultural season October 1989
- h. Adopt the contrat-plan August 1988

**2. Pricing Policy Reform**

- a. Introduce a three-tiered pricing system, each price being linked to a particular quality of seed cotton July 1988
- b. Define the rules of operation for the new flexible pricing system November 1988
- c. Establish guidelines for the operation and replenishment of the price support fund November 1988
- d. Lower the floor price for the 1989/90 and 1990/91 seasons March 1989

**3. Agricultural Policy**

- |   |               |
|---|---------------|
| a. Reformulate the 1988/89 production plan to favor the efficient region  | February 1988 |
| b. Formulate program to reduce input costs and enlarge the choice of inputs available to the farmer while continuing full cost pricing of agricultural inputs     | April 1988    |
| c. Redefine the responsibilities of key institutions (ONDR, IRCT, COTONTCHAD) to ensure better coordination and improved efficiency; reorient their work programs | June 1988     |

**4. Settlement of COTONTCHAD's Arrears**

- |   |                                |
|---|--------------------------------|
| a. Reduce the arrears from CFAF 43 billion (Oct 1986) to CFAF 30.6 billion (Oct 1988) | November 1986-<br>October 1988 |
| b. Establish a financing plan to settle arrears                                       | To begin in<br>November 1988   |

**III. Studies to prepare Future Reforms**

- |  |  |
|--|--|
| a. Undertake diagnostic studies of five important public sector enterprises                  | Before end<br>1988                     |
| b. Undertake studies of additional public sector enterprises                                 | Studies to<br>begin before<br>end 1988 |
| c. Undertake study of cross arrears of parastatals   | Before end<br>1988                     |
| d. Prepare a study of the composition, configuration and efficiency of public administration | Before end<br>1989                     |

Attachment 2

CHAD - Budgetary Procedures

With regard to the budgetary amendment, designed to increase operating expenditures (excluding personnel) of eight ministries, the monitoring procedure for real expenditures will be as follows. The Government (i) will set up a system of special "bordereaux" for each ministry, and (ii) will prepare a semi-annual report to which detailed tables will be attached signed by the Central Treasurer, the Budget Director and the Director of the technical ministry concerned. These tables will supply the following information for each budgetary line subject to the budgetary amendment:

- total budget allocation (initial allocation and supplementary financing)
- total committed
- total payment
- balance and implementation rate

## CHAD: Public Sector Financing Plan, 1987-89

## Attachment 3

(millions of CFAF)

|  | 1987<br>est.    | 1988<br>1st sem. | 1988<br>2nd sem. | 1988            | 1989            |
|--|-----------------|------------------|------------------|-----------------|-----------------|
| <b>CENTRAL GOVERNMENT</b>                                      |                 |                  |                  |                 |                 |
| Revenues   | 19,497          | 9,625            | 12,591           | 22,216          | 24,325          |
| Expenditures   | 78,677          | 38,945           | 45,044           | 83,989          | 92,010          |
| Current expenditures   | 27,677          | 11,445           | 17,344           | 28,789          | 30,610          |
| operating expend. in 8 ministries 1/                           | 297             | 250              | 1,750            | 2,000           | n.a             |
| government budget  | 297             | 250              | 250              | 500             | n.a             |
| supplemental budget  | 0               | 0                | 1,500            | 1,500           | 1,165           |
| Capital expenditures   | 51,000          | 27,500           | 27,700           | 55,200          | 61,400          |
| pipeline projects  | 51,000          | 27,500           | 26,900           | 54,400          | 53,400          |
| new projects   | 0               | 0                | 0                | 0               | 6,200           |
| government counterpart funds                                   | 0               | 0                | 800              | 800             | 1800            |
| Variation in Central Government arrears                        | 502             | (943)            | (1,388)          | (2,331)         | (1,500)         |
| Teachers' salaries   | 13              | 0                | (230)            | (230)           | 0               |
| Other Internal   | 489             | (750)            | (1,158)          | (1,908)         | (1,500)         |
| External   | 0               | (193)            | 0                | (193)           | 0               |
| Central Government deficit<br>(on a cash basis)                | <u>(58,678)</u> | <u>(30,263)</u>  | <u>(33,841)</u>  | <u>(64,104)</u> | <u>(69,185)</u> |
| <b>PUBLIC ENTERPRISES</b>                                      |                 |                  |                  |                 |                 |
| COTONTCHAD operating deficit                                   | (4,109)         | (588)            | (589)            | (1,177)         | (6,992)         |
| Reduction in COTONTCHAD arrears                                | (7,700)         | (1,700)          | (9,316)          | (11,016)        | (8,200)         |
| Combined Central Govt./COTONTCHAD deficit<br>(on a cash basis) | <u>(70,487)</u> | <u>(32,551)</u>  | <u>(43,746)</u>  | <u>(76,297)</u> | <u>(84,377)</u> |
| <b>FINANCING</b>   | <u>70,487</u>   | <u>33,149</u>    | <u>43,148</u>    | <u>76,297</u>   | <u>79,783</u>   |
| External   | 68,973          | 33,149           | 43,454           | 76,603          | 81,134          |
| Project assistance (PIP)                                       | 51,000          | 27,500           | 26,900           | 54,400          | 59,600          |
| pipeline projects  | 51,000          | 27,500           | 26,900           | 54,400          | 53,400          |
| new projects   | 0               | 0                | 0                | 0               | 6,200           |
| Non-project assistance   | 18,418          | 6,123            | 17,028           | 23,151          | 22,634          |
| United States  | 1,609           | 750              | 750              | 1,500           | 1,631           |
| France   | 9,099           | 3,000            | 7,010            | 10,010          | 4,010           |
| Ministry of Cooperation  | 5,382           | 3,000            | 4,408            | 7,408           | n.a             |
| CCCE   | 3,717           | 0                | 2,602            | 2,602           | 4,010           |
| World Bank   | 1,600           | 0                | 6,500            | 6,500           | 6,782           |
| African Development Bank                                       | 0               | 0                | 1,268            | 1,268           | 7,841           |
| Netherlands  | 0               | 673              | 0                | 673             | 2,370           |
| European Economic Community                                    | 6,110           | 1,700            | 1,500            | 3,200           | n.a             |
| STABEX   | 4,410           | 1,700            | 1,500            | 3,200           | n.a             |
| Fifth EDF  | 1,700           | 0                | 0                | 0               | 0               |
| Repayment of ext. debt (incl. debt relief)                     | (445)           | (474)            | (474)            | (948)           | (1,100)         |
| Internal   | 1,514           | 0                | (306)            | (306)           | (1,351)         |
| Banking system   | 439             | 0                | (306)            | (306)           | (1,351)         |
| Non-banking system   | 1,075           | 0                | 0                | 0               | 0               |
| Financing Gap  | (0)             | (598)            | 598              | 0               | 4,594           |

1/ Development ministries targetted under the FRC include Public Health, Education, Social Affairs, Public Works, Transport, Agriculture, Tourism/Environment, and Livestock.

FRC POLICY MATRIX

| Policy areas and Objectives   | Measures  | Status of Preparation                       | Implementation date                               |
|---|---|---|---|
| <b>I. Public Sector Resource Management</b>                               |   |   |   |
| <b>1. Public Investment Program (PIP)</b>                                 |   |   |   |
| Improve efficiency of public investment                                   | a. Adopt 1988 PIP   | completed                                   | January 1988                                      |
|   | b. Prepare studies on specific projects:<br>- sugar<br>- irrigation   | completed                                   | March 1988  |
|   | c. Adopt rolling PIP for 1989-91  | underway                                    | January 1989                                      |
|   | d. Strengthen PIP preparation and evaluation process  | underway                                    | June 1988   |
|   | e. Formulate sectoral strategies:<br>- Livestock<br>- Transport<br>- Education<br>- Health                                | completed<br>completed                      | 1988-1989<br>1988<br>1988<br>end 1988<br>end 1989 |
|   | f. Hold sectoral aid coordination meetings<br>- Agriculture<br>- Transport<br>- Education                                 | completed<br>completed<br>under preparation | December 1988<br>February 1988<br>mid-1989        |
| <b>2. Operating Budget</b>  |   |   |   |
| Enhance operational capacity of key ministries/agencies for development   | a. Increase non-personnel operating expenditures for second semester 1988 in 8 target ministries                          | Budget amendment prepared                   | July 1988   |
|   | b. Prepare 1989 budget, including increased non/personnel operating expenditures for the 8 ministries                     | underway                                    | December 1988                                     |
|   | c. Strengthen expenditure authorization and monitoring procedures   | initial measures taken                      | February 1988                                     |
| <b>3. Fiscal Policy</b>   |   |   |   |
| Increase government revenues and improve the efficiency of the tax system | a. Replace differentiated petroleum import tax system with unitary consumption tax to increase revenues in the short term | completed                                   | July 1987   |
|   | b. Reinforce collection and recovery efforts of petroleum tax   | completed                                   | November 1987                                     |
|   | c. Prepare an overall study of fiscal system, including special funds   | IMF is preparing TORs                       | Study to be completed before the end of 1988      |

| Policy area and Objectives   | Measures  | Status of Preparation   | Implementation date   |                                       |
|--|---|---|---|---------------------------------------|
| <b>II. Cotton Sector</b>   |   |   |   |                                       |
| <b>1. Restructuring of Cotton Sector</b>   |   |   |   |                                       |
| Improve efficiency, reduce financial risks and improve the long term financial viability of the sector | a. Reform pricing policy<br>- differentiate price according to three qualities<br>- adopt rules for operation of new pricing system<br>- lower floor price for 1988/89 and 1989/90 seasons  | completed<br>under preparation<br>under preparation                                 | 88/89 agricultural season<br>November 1988<br>March 1989            |                                       |
|  | b. Create price support fund within COTONCHAD   |   | November 1988   |                                       |
|  | c. Reformulate the 1988/89 production plan to favor the efficient region  | completed   | February 1988   |                                       |
|  | d. Formulate program to reduce input costs and enlarge the choice of inputs available to the farmer while continuing full cost pricing of agriculture inputs  | completed   | April 1988  |                                       |
|  | e. Identify additional measures for reducing COTONCHAD's costs and improving its management capacity<br>- transfer COTONCHAD financial and administrative services to Moundou<br>- adopt revised organization structure<br>- create input management office<br>- adopt program to improve oil and soap production | underway<br>proposal prepared<br>underway   | 1988-1989<br>May 1989<br>October 1988<br>July 1988<br>November 1988 |                                       |
|  | f. Adopt "contract-plan" for COTONCHAD  | prepared  | August 1988   |                                       |
|  | g. Redefine the responsibilities of key institutions (ONDR, IRCT, COTONCHAD) to ensure better coordination and improved efficiency; reorient their work programs  | agreement finalized   | June 1988   |                                       |
|  | <b>2. Settling COTONCHAD's Arrears</b>  |   |   |                                       |
|  | Improve the financial viability of COTONCHAD and increase Chad's access to Central Bank credit  | a. Reduce arrears from CFAF 45 billion (Oct. 1986) to CFAF 36.6 billion (Oct. 1988) | First-year payments of CFAF 7.7 billion made                        | November 1988-<br>October 1988        |
|  |   | b. Establish a financing plan to settle arrears                                     | Proposal under negotiation with Central Bank                        | Implementation to start November 1988 |

| Policy areas and Objectives | Measures | Status of Preparation | Implementation date |
|-----------------------------|----------|-----------------------|---------------------|
|-----------------------------|----------|-----------------------|---------------------|

III. Studies to Prepare Future Reforms

|   |  |                                |                                 |
|---|--|--------------------------------|---------------------------------|
| Prepare studies on rationalizing public enterprise sector | a. Undertake diagnostic studies for five important public enterprises                        | Bidding underway               | Studies to be completed in 1988 |
|   | b. Undertake studies for additional public enterprises                                       |                                | Studies to begin in late 1988   |
|   | c. Undertake study of cross arrears of parastatals   | TORs agreed                    | Study to be completed in 1989   |
| a. Public Administration                                  | a. Prepare a study of the composition, configuration and efficiency of public administration | TORs to be drafted by mid-1988 | Study to be completed in 1989   |

