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ADJUSTMENT POLICIES IN THE IVORY COAST IN THE FRAMEWORK OF UMOA

Kathie Krumm

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"Adjustment Policies in the Ivory Coast in the Framework of UMOA"

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This paper is written as an input into the Ivory Coast Country Economic Memorandum 1985. In response to a number of adverse developments, the Ivory Coast is currently undergoing a process of adjustment. One of the prominent features of the Ivory Coast economy is that the country is a member of a currency union, the West African Monetary Union (Union Monetaire de l'Afrique de l'Ouest or UMOA). This paper analyzes UMOA's operations and its impact on the adjustment process.

While the real exchange rate for the Ivory Coast has depreciated, the relative price movements have not been sufficient to generate both internal and external balance. Yet policies facilitating real exchange rate adjustment have to be evaluated in the context of the currency union. Importantly, the currency of the union is pegged to the French franc, contributing to the stability of the system but making the nominal exchange rate exogenous. One must look toward other instruments and developments that affect overall price trends and relative prices.

Monetary developments of course play a key role. The first part of the paper outlines the features of UMOA's monetary system and the supposed mechanisms of adjustment to external imbalances, setting the stage for a discussion in the second section of the actual monetary developments in the Ivory Coast from 1981 to 1984 and the relative price trends over the same period. The Ivory Coast's inflation rate declined but remained at levels above those of France, so that the major factor contributing to any

depreciation of the real exchange rate has been the depreciation of the French franc. In addition, a large proportion of tradables prices facing producers are fixed and have not risen in line with the depreciation, with the increased export margin accruing to the government. In the final section, the implications of continuing the existing process are outlined, including reliance on automatic balance of payments support through drawings on an account with the French Treasury and on external debt reschedulings and suggesting the consideration of an additional focus on relative prices.

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I. Introduction

In response to a number of adverse developments, the Ivory Coast is currently undergoing a process of adjustment. One of the prominent features of the Ivory Coast economy is that the country is a member of a currency union, the West African Monetary Union (Union Monetaire de l'Afrique de l'Ouest or UMOA).[1/] To understand better the medium-term adjustment issues facing the Ivory Coast, it is crucial to analyze UMOA's operations and its impact on the adjustment process.

This paper is motivated by two main concerns. While the real exchange rate for the Ivory Coast has depreciated, the relative price movements have not been sufficient to generate both internal and external balance. Without sufficient switching of expenditures and production, balance of payments equilibrium can be attained only through further across-the-board expenditure reduction which inhibits growth or unsustainable debt accumulation.

The second motivation is the importance of evaluating policies facilitating real exchange rate adjustment in the context of the currency union. Importantly, the currency of the union is pegged to the French franc, contributing to the stability of the system but making the nominal exchange rate exogenous. One must look toward other instruments and developments that affect overall price trends and relative prices.

Monetary developments of course play a key role. In the next section, the paper briefly outlines the features of UMOA's monetary system,

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1/ Other members of the union are Benin, Burkina, Mali, Niger, Senegal and Togo.

including the major instruments of monetary control and the process of setting the monetary policy. The emphasis is not on the efficacy of the monetary instruments, although UMOA's difficulties with monetary control given the openness of the economy and various public sector leakages are mentioned. Rather the emphasis is on the absence in the process of any attempt to harmonize the relative level of prices with medium-term balance of payments considerations.

This sets the stage for a discussion of the monetary developments in the Ivory Coast from 1981 to 1984 and the relative price trends over the same period. To a considerable extent, the negative monetary impact of adverse balance of payments developments (including terms of trade deterioration, high international interest rates and drought) was sterilized by the central bank, largely through domestic credit extended to the public sector. The Ivory Coast's inflation rate declined but remained at levels above those of France. The major factor contributing to any depreciation of the real exchange rate has been the depreciation of the French franc. In addition, a large proportion of tradables prices facing producers are fixed and have not risen in line with the depreciation, with the increased export margin accruing to the government, and thus, it is not surprising that there has not been more of a medium-term production response to the real exchange rate depreciation.

In the final section, the implications of continuing the existing process are outlined, suggesting the consideration of an additional focus on relative prices. The Ivory Coast has had to rely increasingly on automatic balance of payments support through drawings on an account with the French Treasury and on external debt reschedulings, which cannot be expected to remain permanent instruments for balance of payments adjustment. Yet

adjusting relative prices through monetary policy given the low levels of expected world inflation implies a difficult deflationary policy option. The paper concludes with a plea for more serious consideration of altering certain key fixed tradables prices so that any required deflation can be limited to the non-tradables sector.

II. The UMOA System

The currency union to which the Ivory Coast belongs, UMOA, has a number of features with implications for the adjustment policies followed by the Ivory Coast 1/. The first one discussed below is the fixity of the exchange rate with the French franc and the special arrangement with the French Treasury for maintaining convertibility. Within this framework, the central bank, the BCEAO, has a variety of instruments for exercising monetary control. Although its control is limited because of the openness of the economy, the BCEAO sets yearly targets for both the union as a whole and the individual members aimed at a short-term balance of payments result, but, as argued below, there are a number of weaknesses in the process that could hamper the medium-term adjustment process.

A. The Exchange Rate

The common currency of UMOA, the CFA franc, is pegged to the French franc. The CFA franc for West Africa is issued by a common central bank, the Banque Centrale des Etats de l'Afrique de l'Ouest (BCEAO), which buys and sells it at a fixed rate for French francs. The Council of Ministers of Finance has ultimate authority for the policy of the central bank. The Board of Directors consists of two representatives from each member country and France and is responsible for the daily operations. In addition, a National Credit Committee headed by the Minister of Finance in each member country has domestic authority on a limited set of issues.

1/ The major sources of material presented in this section are Guillaumont (1984), Bhatia (1982), World Bank (1981) and various documents of the BCEAO.

The exchange rate has remained unchanged since 1948 at 50 CFA to 1 French franc. 1/ Parity can be changed only by unanimous agreement of UMOA member countries and France.

Under the current Cooperation Agreement between France and the member states signed in 1973, France agrees to provide support to maintain the free convertibility between the CFA franc and the French franc. The convertibility is maintained through the use of an Operations Account (compte d'operations) which the BCEAO maintains with the French Treasury. When reserves are positive, as they generally were until 1980, the BCEAO is required to keep at least 65% of its foreign currency reserves in French francs deposited in the Operations Account. France provides an exchange rate guarantee for these deposits vis-a-vis the SDR and pays interest equal to the rediscount rate of the Bank of France. Likewise, convertibility can be supported through use of overdraft facilities on the Operations Account which has been the situation for UMOA as a whole since 1980. The interest rate applied to the overdraft rises progressively to the Bank of France rediscount rate, at which it currently stands.

Consistent with the concept of a monetary union, the Operations Account is a pooling of the individual countries' external balances (or overdrafts). The BCEAO maintains separate accounts for each country and credits or charges each country according to its contribution to the pooled account.

France's obligation to support UMOA in maintaining unlimited and full convertibility of the CFA franc is subject to certain restrictions on govern-

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1/ Only from the inception of the CFA in 1945 to October 1948 were there slightly different rates.

ment borrowing from the central bank and the requirement that certain policy measures be taken to retard any dangerous decline in the BCEAO's external asset position. According to the statutes of the BCEAO, whenever the pooled external reserves of the BCEAO fall below 20% of its sight liabilities over three consecutive months, the Board must meet in order to take appropriate decisions regarding monetary policy. These decisions are reached by a simple majority. 1/ The monetary policy adjustments described further below can include reductions in rediscount ceilings and bank credit authorizations as well as further increases in the rediscount rates. Although there are no automatic measures to be taken, unlike the agreement prior to 1974, the BCEAO must act to address the decline. According to the separate Cooperation Agreement, as well as the BCEAO statutes, whenever the Operations Account is depleted, public and private institutions in specified countries can be required to sell their liquid external assets to the BCEAO.2/

1/ A simple majority is required for all Board decisions with the exception of those concerning rediscounts of public sector obligations of 10 years or more and capital participation in development financial institutions which require 6/7s majority usually and unanimity in the situation of low external reserves described above.

2/ While the BCEAO has nc legal relationship with it, the Banque des Etats de l'Afrique Centrale (BEAC) and its agreement with the French Treasury are significant to this analysis. Five countries belong to the Union Douaniere des Etats de l'Afrique Centrale (UDEAC): Cameroon, Gabon, Congo, Central African Republic and Chad. These countries have a common central bank, BEAC, a common currency, also named the CFA franc, and a similar Operations Account at the French Treasury. While BCEAO has recently acquired a sizeable overdraft, BEAC continues to maintain large surpluses in its account, due mainly to the oil revenues of three of its member countries. It has been suggested that the French Treasury takes the overall balance of the two unions into account, in addition to the balance of UMOA alone, when considering the extent of measures to address an Operations Account imbalance.

In summary, under the current UMOA system, the nominal exchange rate for the CFA franc used in the Ivory Coast is pegged to the French franc and correspondingly floats with it in the international market relative to other currencies. For the current discussion, the relevant feature of the agreement by France to support the CFA franc convertibility is that it is handled through an Operations Account with overdraft facilities at near market rates (Bank of France rediscount rate) and that the BCEAO is obligated to pursue policies that restrain usage of such a facility.

B. Instruments of Monetary Control

The BCEAO has a variety of instruments to control the quantity and quality of credit in the member countries. The major ones are limitations on advances to the government, rediscount facilities, and prior authorizations of credits, and others include the interbank money market and potentially reserve requirements. In addition, there are instruments to control the sectoral distribution of credit. 1/ In practice, a number of other factors affect monetary developments and complicate the BCEAO's task of directing monetary policy. Major ones are the financial relationships between the government and both public sector enterprises and external lenders and the possibility of public and private sector arrears, which enter into our discussion of government advances. Another factor is the openness of the Ivorien economy which is discussed in the following section.

1/ This set of instruments has been in place since 1974. For a description of the set prior to 1974, see Bhatia (1982).

1. Rediscount facilities

The BCEAO exercises control primarily through its rediscount facilities. As part of its annual exercise, the BCEAO sets a limit on its financing of credit in each member country. This limit excludes seasonal agricultural credit (credits de compagne), but these credits are tightly supervised in the Ivory Coast to ensure appropriate usage. For all other credits, the BCEAO requires rigid adherence to the ceiling.

The rediscount facilities are allocated between the government and the rest of the economy, including the private sector and the public enterprises. After determining the amount available to the government, the BCEAO subtracts it from the overall ceiling to derive the residual ceiling for the rest of the economy. Within this ceiling, the BCEAO creates ceilings for the individual financial institutions within each member country, although the institutions are not informed of their limits until they have been reached. These ceilings are subject to change by the BCEAO during the year without notice. 1/ The percent of a total bank's credit excluding seasonal credit that is rediscounted is not to exceed 35 percent. 2/

The usage of the rediscount facilities also is influenced by the rediscount rate. The interest rate is set by the BCEAO at the same level for all member countries. In practice, since the initial move toward higher rates in 1973, the rates have been adjusted only four times (in 1975, 1980, 1982 and

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1/ For example, when the central bank notes an increasing reliance on rediscounting and a reduction in other financing sources, such as parent companies (meres), it can react by reducing further the individual financial institution's rediscount ceiling.

2/ Note that this regulation has not been strictly adhered to during the current liquidity crisis in the Ivory Coast.

1983) and have tended to remain substantially below equivalent French rates until recently. By setting ranges for bank margins over and above the rediscount rate, the BCEAO influences lending rates on all credits and deposit rates. The central bank also sets the rate on the small interbank money market which is adjusted more frequently. The evolution of rates is given in Table 1.

The BCEAO also refinances through the use of advances to the banks. Although these are officially discouraged by the sharply accelerating penalty rates which increase 1 percent each day from 10.5 percent to a maximum of 25.8 percent, certain banks recently have been willing to pay these rates. 1/

2. Advances to the government

The government's access to domestic credit is limited by the BCEAO statutes to a fixed percentage of the previous year's fiscal receipts. At the same time, a government's request for credit within this limit cannot be denied easily.2/ Since 1972, the maximum authorized percentage has been 20 percent. The calculation is made based on most recently available fiscal data, which currently translates into a one-year lag for the Ivory Coast, e.g., 1984 limits were based on 1982 revenues. This limit applies not only to advances to the Treasury, but also to rediscounts of and advances against medium-term public bonds, government obligations of up to 10 years for financing development projects, holdings of Treasury bills and credit balances with the postal checking system.

1/ See de Boissieu (1984).

2/ When an IMF agreement is in force with a lower limit, the BCEAO then can deny a request over the IMF limit.

While this statutory limit on the amount of central bank advances to the government is significant in reducing fiscal pressures on the monetary system, three other major avenues exist for government financing. The public sector is comprised not only of the government, but also various public enterprises. In the BCEAO accounts, the public enterprises are included in the private sector category. By reducing its direct financing of these enterprises, the government can encourage these enterprises to borrow within the banking system, often with a government guarantee, thereby allowing larger direct government expenditures and increasing overall public sector borrowing. Second, the government and/or the public enterprises can be in arrears on payments due to the private sector. Third, the government and/or public enterprises can borrow externally without violating UMOA guidelines. As many analysts have concluded, the extent of BCEAO's control is asymmetric, being greater when the public sector's access to external borrowing is restricted.1/

As mentioned, the credit to be extended to the government by the central bank is subtracted from the overall rediscount ceilings to derive the ceiling for the rest of the economy rather than added onto a separately determined ceiling for other credit. Thus, in an important sense, monetary policy does not accommodate fiscal policy. Nonetheless, it becomes increasingly difficult for the BCEAO to restrict credit to the rest of the economy beyond a certain point without serious disruption to the financial soundness of the economy, particularly if the portion of that credit representing indirect government advances through public enterprises or arrears is also large.

1/ An IMF program can encompass all three elements and therefore complements the current range of BCEAO instruments for monetary control related to fiscal policy.

3. Prior authorizations

Another instrument that has grown in importance is the prior authorization (autorisation prealable) from the BCEAO that the banks are required to obtain on any credit to an enterprise over a certain amount, CFAF 100 million for the Ivory Coast. The major purpose of the instrument was to control quality and allocation of credit, although it could be used for influencing overall credit expansion also. One limitation of using it for credit control is that once the central bank gives its authorization, it has no system for monitoring if and how much of the credit has been actually granted.

4. Other

The central bank is empowered to impose reserve requirements on banks, expressed as a percentage of either their deposits or their loans. To date, the BCEAO has not imposed such requirements, but, nonetheless, the ratios of bank reserves held at the central bank have remained steady.

The BCEAO has set up an interbank money market, where banks can deposit excess funds with the central bank which relends them to other banks within the Union. In addition to reducing capital outflows, the BCEAO can use the money market to control the money supply either by placing excess funds on the French money market or by meeting excess demand through overnight advances (which has been the situation). The interest rates are determined by the BCEAO, and in general, exceed the rediscount rate and fall short of the French interbank rate, as shown in Table 1. 1/ The Ivory Coast banks have been major net borrowers in this interbank market, but the market remains small.

1/ Also the central bank can refuse to rediscount to banks with money market deposits whenever the money market rate exceeds the rediscount rate.

5. Selective credit instruments

The BCEAO has two main instruments to influence the sectoral distribution of credit, a preferential interest rate structure and minimum/maximum lending ratios for certain sectors. The sectors eligible for preferential rates and the structure of those rates are determined for the Union as a whole. Currently there are three priority areas: seasonal agricultural credit, loans to small- and medium-sized national enterprises, and loans for social housing construction. These credits can be rediscounted at a preferential rate, currently 2 1/2 percent below other rates, and, allowing banks a margin between 1 and 3 percent compared to an ordinary margin of 0 to 5 percent, carry a preferential interest rate for the borrower as well. The majority of these credits when granted are rediscounted. The structure of rates is given in Table 1.

The minimum/maximum sectoral lending ratios are determined on an individual country level by the National Credit Committee. It is important to note that these ratios are indicative and not binding. The BCEAO has been reluctant to penalize banks not meeting these targets. Specified sectors in the Ivory Coast currently include small- and medium-sized enterprises and social housing, similar to the Union-wide preferential rates categories, as well as specified public enterprises in petroleum, rail, gas and water. In addition, as of March 1983, a maximum ratio was set for construction in the Ivory Coast, which is easier for the BCEAO to enforce through its prior authorization system than a minimum ratio.

C. Openness of the Economy

The workings of the monetary union can only be understood in the context of the overall openness of the economies of the Union. The most extreme openness is with respect to other countries within the French franc zone. The latest Cooperation Agreement between UMOA and France affirmed the principle of free and unrestricted capital flows not only within UMOA but also with France. 1/ The transfers, without quantitative limits, are subject only to a tax of 0.25 percent. Although certain reporting and approval mechanisms have been set up by both the BCEAO and the Ivorian government, capital flows to and from countries outside the franc zone also have few unrestrictions. The central bank is informed of such transactions and assists in harmonizing the exchange controls of the different members. From the Ministry of Finance of the Ivory Coast, prior approval for non-franc zone transfers must be obtained except for those related to short-term advances, but there is no system to monitor whether such transfers occur. Regardless, to the extent flows between UMOA and France are unrestricted, the restrictions on the capital account essentially are those defined by the Bank of France for transfers between France and non-franc zone countries. From May 1981, the French exchange controls became much stricter but are now beginning to ease. This openness of the Ivory Coast's economy limits the monetary and credit control that the BCEAO can exercise over the private sector as well as the private sector and complicates its task.

1/ This is qualified by a clause that allows a change for a member country should the circumstances necessitate such, as determined by all signatories.

D. Yearly Monetary Policy Setting Process

As monetary and credit developments affect adjustment, it is useful to understand how monetary authorities set policy. The core of this process is an annual determination of global targets for UMOA's overall position and monetary and credit targets for each member country consistent with the global picture. The first stage is carried out primarily by BCEAO headquarters while the second is a process of iteration and negotiation involving the Council of Ministers, the National Credit Committees and the BCEAO. Both the global and individual country targets must be agreed upon unanimously by the Council of Ministers.

In setting global targets, the BCEAO has as its primary objective the maintenance of a certain level of net external assets and thus a balance of payments result. While there is no rigid relationship between an individual member's accumulated position and its target, a country which contributed to the decline in the net external asset position of UMOA would be targetted to achieve some degree of corrective action. This is expressly the case when a member's net external asset position has deteriorated to less than 20 percent of total sight liabilities, as is the case of the Ivory Coast since 1980.

The eventual monetary and credit components are basically residuals derived from a consistency framework based on the balance of payments target. While the process is obviously iterative and political, the BCEAO has outlined eight basic steps:

(1) estimation of the growth rate of GDP volume from estimated rates of the agricultural, mineral, manufacturing and tertiary sectors;

(2) forecast of the general price level based on forecasts of import and export prices (taking into account inflation rates of major trading

partners) as well as trends in prices of non-tradeable domestic goods, as long as this general absolute level of inflation (as opposed to the level relative to trading partners) does not appear excessively high;

(3) estimation of the major public finance components to determine the portion of the Treasury deficit to be financed through the financial system, where these estimates are made consistent with estimates of GDP, exports and imports as they affect revenues and public sector external borrowing and aid flows;

(4) establishment of targets for various balance of payments components, where imports are based on recent sectoral import coefficients and external price variations, where exports are based on product-specific information, and where net capital flows are based on best judgments of availability;

(5) determination of the desired stock of money based on the quantity theory of money, assuming a velocity consistent with recent trends;

(6) distribution of the stock of money into its various components assuming a given ratio of currency to deposits;

(7) determination of the growth of net domestic credit from the targetted growth in money and net foreign assets and its distribution between public and private sector based on the projected public finance component with private net domestic credit as a residual;

(8) derivation of the situation of the financial sector, both deposit banks and the central bank, from the monetary, fiscal and balance of payments components, based on a stable bank reserve coefficient and credit multiplier among other things.

Because this annual process merely serves as a benchmark from which to make decisions, its shortcomings should not be overemphasized. However, it

is useful to point out certain weaknesses with particularly strong implications for medium-term adjustment.

First, the process only attempts to encompass developments over one year and therefore does not take into account the implications of the derived policies over the medium term. The balance of payments situation as it evolves in the medium-term is not an explicit concern of the current BCEAO process for policy setting.

Second, monetary and credit policy of the BCEAO are determined passively and not viewed as active instruments for influencing certain variables that affect adjustment on the real supply side of the economy. A notable example is relative prices, which are variables emphasized in this paper. The method treats monetary policy as accommodating to expected inflation rates as long as that absolute level is not excessively high or in line with that of France, rather than viewing it as instrumental in harmonizing the relative level of inflation with balance of payments considerations.

III. Monetary and Relative Price Developments 1981-84

Based on the preceding description of the UMOA system, this section of the paper describes the developments in the Ivory Coast from 1981 to 1984. The background section suggests certain strengths and limitations of the system for both assisting the Ivory Coast economy in adjusting to the primarily adverse shocks that it faced and encouraging developments consistent with UMOA's short-term net external position objectives.

In the presence of balance of payments difficulties, either negative real shocks or credit rationing, one strength is that the monetary control exercised by the BCEAO would be greater, as the financial system and government rely increasingly on the central bank's rediscount facilities, if it chose to exercise the control. At the same time, in a tight monetary situation, the government could be expected to take the lion's share of credit, borrowing from the central bank up to its statutory limit, and then turning to its public enterprises and accumulation of arrears.

Another strength is that the Operations Account provides a cushion and would be expected to come under heavy usage during periods of balance of payments difficulties. Nonetheless, for shocks not of a temporary nature, a relative price (i.e., real exchange rate) adjustment would be necessary, but such medium-term considerations would not be expected to be integrated into the monetary policy setting process of UMOA. As described below, these four predicted developments, i.e., slower monetary growth, absorption by the public sector of a large share of domestic credit, heavy usage of the Operations Account, and finally an evolution of relative prices insufficient for medium-term balance of payments equilibrium, were dominant characteristics of the Ivory Coast economy in the 1980s.

A. Background

During the first two decades after independence in 1960, the Ivory Coast attained relatively high rates of growth in both GDP and agricultural production. The stimulus in the late 1970s was primarily a boom in both coffee and cocoa prices, the country's two major exports which comprise roughly half of total exports. A massive public investment program that was launched in response to the surpluses in the agricultural stabilization fund contained a number of large, poorly conceived projects and increasingly was financed by external borrowings as the export prices precipitously returned to pre-boom levels.

By the end of 1980, the continuing worsening prospects for the terms of trade, the sharp increase in the cost of external borrowing and the accumulation of domestic payment arrears led to a financial recovery plan in the context of a three-year extended arrangement with the Fund. In making an agreement with a UMOA member country, the Fund also reached agreement with the BCEAO on the setting of monetary and credit ceilings and sub-ceilings.

Because the main body of the Country Economic Memorandum contains a detailed account of the macroeconomic developments from 1981-84, this section outlines only the major trends and highlights the impact of the UMOA system on the monetary developments in the Ivory Coast.

B. Monetary Policy in Practice

1. Developments in 1981-82

a. Nominal exchange rate

The appreciation of the US dollar that had begun in 1980 accelerated sharply in 1981 and continued in 1982. The French franc (and therefore the CFA franc) depreciated nominally vis-a-vis the dollar by 27 percent in 1981

and a further 17 percent in 1982. As shown in Table 2, the import-weighted nominal exchange rate index for the Ivory Coast rose 6 percent in 1981 and 8 percent in 1982 and its export-weighted index rose 6 percent and 4 percent, respectively. Since Ivory Coast has its external debt denominated in various currencies, with about a half in US dollars, the dollar appreciation resulted in a sizeable and largely unexpected increase in the debt service.

b. Net foreign assets

As shown in Table 3, net foreign assets fell by CFAF 145 billion in 1981 and another CFAF 45 billion in 1982. The 1981 balance of payments deficit proved larger than had been expected during the formulation of monetary and credit policy due to three major factors. First, the terms of trade deteriorated by more than expected, by over 12 percent, and, in addition, the imposition of coffee export quotas reduced exports. Nonetheless, the country showed an increased trade surplus. Second, interest payments on external debt were higher from both the depreciation of the CFA franc against the dollar and the high international rates. These two factors led to a current account deficit of CFAF 330 billion, representing 14 percent of GDP, more than the 1980 deficit, as shown in Table 4. Third, the reluctance of the BCEAO to adjust the structure of interest rates further in response to the sharp increases in international rates contributed to a reversal of monetary flows to a net outflow in 1981. With the lending rate ceiling at 15.5 percent and international rates at about 20%, Ivorian banks moved to reduce their international borrowings to avoid unprofitable margins. Although the Ivory Coast had been pushing for higher rates at the BCEAO, it was obliged by the UMOA system to enforce the rates set by the overall Union.

Balance of payments pressures continued in 1982. On the trade side, terms of trade decreased again, and the domestic oil sector contributed less

than originally expected, but strong trade surplus performance was maintained. However, interest payments on public external debt continued to jump, resulting in a current account deficit of again about 14 percent of GDP. The capital account pressures eased considerably as the BCEAO raised the discount rate and therefore the lending rate ceiling by 2 percent and international rates dropped more in line with those set by the BCEAO. Also, sizeable non-project loans were dispersed, but these net inflows were not sufficient to offset the current account deficit. After these two years of continuing balance of payments deficits, the net negative foreign asset position of the Ivory Coast exceeded CFAF 430 billion.

c. Domestic credit

In the area of net domestic credit over which the monetary authorities have more direct influence, the levels for 1981 and 1982 were near those targetted in the policy formulation stage. In other words, the monetary authorities did not respond to the increase in the net external liabilities by completely sterilizing its effect.

The growth of net domestic credit as defined by the BCEAO which had been increasing from 1978 to 1980 slowed slightly in 1981 to 23.1 percent, and more sharply according to the Fund definition, as shown in Table 3. 1/ Largely because of the recession, the private sector demand for credit weakened. In addition, there was increasing demand for the BCEAO's refinancing facilities, and therefore it was easier for the central bank to tighten credit. As shown in Table 5, the percent of total credit refinanced increased to 39 percent in 1981 from 31 percent in 1980 and 26 percent in

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1/ Note that year-end to year-end changes need to be interpreted with caution because of strong seasonal movements and variable agricultural financing.

1979, and the percent of ordinary credit refinanced increased to 24 percent from 16 percent and 19 percent, respectively. Non-government credit rose 8.6 percent. The public sector depended heavily on central bank financing as well and moved from a net creditor to a net debtor position. The government's use of BCEAO facilities is tightly proscribed by the UMOA statutes as explained earlier.

Net domestic credit growth slowed considerably in 1982 to 6.8 percent. Private demand remained low because of both the increased interest rates and the worsened recession particularly as it expanded to the agricultural sector. The BCEAO again maintained control through use of its refinancing facilities which financed 40 percent of total credit and 28 percent of ordinary credit. To finance its deficit and domestic arrears repayment, the government turned largely to foreign borrowing (80 percent of its requirements) in 1982, unlike in 1981, but its net domestic credit still increased 25 percent.

Overall, for 1981-82, the central bank and government slowed monetary growth. This was accomplished primarily by partial sterilization of adverse external developments in 1981 and by continuing restrictive private domestic credit policies in 1982. Monetary growth rates for 1981 and 1982 were 7.7 percent and 5.2 percent, respectively, compared to recent historical rates of 15 percent and 8 percent using the Fund definition. 1/

1/ Using the BCEAO definition, the money growth rate for 1981 actually was higher than in 1979-80.

2. Developments in 1983

a. Exchange rate and net external assets

After an improvement in 1982, the balance of payments deficit deteriorated again in 1983 and ended at close to CFAF 200 billion. Some of the sources of the deterioration had become evident to the authorities earlier, including the weakened oil prospects and the high interest charges on external debt. However, 1983 also evidenced an unexpected fall in the value of exports, due to the effects of drought on agricultural production. This was despite a slight improvement in the terms of trade and a further 24 percent depreciation of the French franc against the dollar. Only the continuing decline in imports contributed to an increase in the trade balance, and after services, the current account was lower than previous years, below 13 percent of GDP.

Another factor in the balance of payments deterioration was the shift in the government's policy toward domestic financing through the central bank of its deficit, unlike 1982, and gross official external borrowing was halved. Combined with sizeable amortization payments, this led to a sharp drop in net capital inflows. Monetary capital inflows though remained steady because of the increasingly competitive deposit rates Ivorian banks had been able to offer when the BCEAO lowered deposit rates less than it lowered the discount and lending rates in response to the easing of international rates.

b. Net domestic credit

Despite a further series of austerity measures, the public sector deficit was adversely affected by the severe drought which hit not only agriculture but also hydroelectric power and thus industry. That, combined with the public sector financing policy, put increasing pressure on domestic credit, with the public sector taking 60 percent of the total and the private

sector allocated the remainder. The BCEAO restrictive rediscounting was maintained, and the share of private credit using central bank refinancing facilities increased to 41 percent of total and 33 percent of ordinary credit. In addition, sizeable arrears to the private sector accumulated and indirectly absorbed more of the private credit. It appears that the BCEAO has increased its use of its prior authorizations instrument up to this point. While the percentage of requests for prior authorizations that was granted dropped to 47 percent in 1983 from previous levels of 79 percent and 92 percent, this is entirely due to flucuations in the seasonal agricultural credit as shown in Table 6. Approval levels for other sectors remain at about 95 percent.

Thus, in 1983, monetary expansion was again dampened by both additional adverse developments and restrictive BCEAO policy. Year-end monetary aggregates grew at rates of 5.8 percent and 5.3 percent under the Fund and BCEAO definitions, respectively.

3. Developments in 1984

a. Debt rescheduling and net external assets

The developments in 1981-83 had placed increased pressure on the balance of payments despite a vigorous program of fiscal and monetary discipline. It became evident a debt rescheduling would be necessary to restore some equilibrium to the 1984 balance of payments. The Ivory Coast government approached its London Club creditors, and agreement was reached in 1984 to reschedule CFAF 211 billion and to inject CFAF 50 billion in new money. This rescheduling is the major factor that will contribute to balance of payments equilibrium in 1984 after several deficit years. There were also sizeable disbursements of non-project loans from the World Bank and CCCE.

Unfortunately the 1983 drought reduced 1984 production more seriously than expected. However, it will be slightly offset by continued favorable shifts in the terms of trade. Recent good weather and producer price rises should increase other agricultural production. The trade surplus for 1984 is estimated by the BCEAO at double its 1981-83 levels, reducing the current account deficit to 6 percent of GDP.

b. Domestic credit

In setting monetary policy, the BCEAO continued to seek a rate of inflation equivalent to that of France and set its monetary and credit targets accordingly. Given the external balance targets, domestic credit remained very tight in 1984. As of July 1984, as shown in Table 3, private sector credit had fallen, primarily due to seasonal agricultural stock financing but also due to similar trends in ordinary credit. The liquidity of the banks was affected by hesitation of foreign lenders, including foreign parent banks, and this was exacerbated by the BCEAO whose refinancing policy remains the same. As of July 1984, the share of credit refinanced by the central bank was unchanged from July 1983. The public sector net claims are targetted to increase only slightly, and, as of July, they had fallen. The public debt rescheduling implies a lower domestic financing requirement. However, indications are that the actual public domestic financing share is larger than these figures indicate because of the continuing accumulation of public sector arrears. This changes the composition but not the level of domestic credit creation which primarily is of concern here.

In summarizing, the BCEAO was by and large successful in attaining lower rates of monetary growth in the Ivory Coast during the 1981-84 period. It was particularly on target in terms of domestic credit expansion based mainly on its use of its refinancing facilities and, to a lesser extent, its

rediscount and related rates. On the other hand, part of its success is attributable to external developments which had large negative impacts on the balance of payments, i.e., terms of trade, interest rate shock and drought, only partly offset in 1982 with external government borrowings and again in 1984 with debt rescheduling. As discussed earlier, the BCEAO's control is asymmetric, being much greater in times of balance of payments difficulties when liquidity in the financial system is declining and banks have to resort more to the rediscounting facilities.

Thus, the slowdown in monetary growth was combined with failure to achieve balance of payments equilibrium before 1984, when debt was rescheduled to alter the profile of the problem. The next section examines whether the development of relative prices over this same period were consistent with alleviation of the balance of payments situation.

C. Relative Price Developments 1981-84

An important question is the extent to which the policies pursued in the Ivory Coast have resulted in a satisfactory evolution of the real exchange rate (defined as the relative price of tradables to non-tradables or the relative price of foreign goods to home goods). Without a sufficient real exchange rate depreciation inducing expenditure-switching, either a country would continue to generate a balance of payments deficit or it would have to rely solely on the reduction of expenditures below the full employment level to eliminate the payments deficit. This is the dilemma now facing the Ivory Coast.

Under the UMOA system, the nominal exchange rate is exogenous. One way the real exchange rate can adjust is vis-a-vis the non-franc zone through a real depreciation (or appreciation) of the French franc against other major

currencies. Another avenue for adjustment is through differences in general price changes in the Ivory Coast compared to other countries including France. At the same time, monetary and fiscal policy aimed at slowing the rise in the price level may have a delayed effect because of the downward stickiness of prices of non-tradables. Likewise, nominal exchange rate depreciation may have a muted effect because of the fixed nature of certain prices of tradables.

Each of these factors is relevant to the evidence for the Ivory Coast in the 1981-84 experience, and help to explain the conflicting trends in the evolution of the real exchange rate. Based on comparisons of general prices indices and nominal exchange rates of the Ivory Coast and its major trading partners, the evidence indicates a depreciation of the real exchange rate due to the depreciation of the French franc, although vis-a-vis the French franc, the Ivory Coast's real exchange rate has appreciated somewhat. However, an analysis based on disaggregated sector price data does not give strong indications of a real exchange rate depreciation. Overall price trends, based on both consumer and producer price indices, responded sluggishly to the tightened monetary situation, and non-tradables price rises remained well above monetary growth rates. More importantly, prices facing producers in the tradables sectors consistently rose less than those in the non-tradables sectors, with the exception of the sharp rise in food crop prices in 1983 due to the drought conditions. The major factor has been the low increase in the fixed producer prices of mainly export crops, where the depreciation has been reflected instead in the export margin captured by the government. This mixed picture of the evolution of relative prices is an important input into the policy analysis that follows.

1. Prices relative to major trading partners

On a basic purchasing power parity basis, the real exchange rate of the Ivory Coast has been depreciating steadily since 1980. 1/ The results for both import- and export-weighted indices are given in Table 2. From 1980 to 1083, the real import- and export-weighted indices depreciated by 25 percent and 23 percent respectively, deflating by consumer price indices, and 17 percent and 17 percent respectively based on GDP deflators. A comparison to data for France indicates the sizeable extent to which this trend is related to the depreciation of the French franc vis-a-vis both the U.S. dollar and the other major currencies of the EMS. In relation to the French franc, the real effective exchange rate for the Ivory Coast appreciated slightly by 11 percent and 6 percent between 1980 and 1983, based on relative consumer price indices and GDP deflators, respectively.

While inflation abated during this period, overall prices appear to have responded sluggishly to the tightening monetary situation described in the last section. Changes in the prices indices lag changes in the monetary growth rates, as shown in Table 7, but there are serious weaknesses in the consumer price indices. 2/ Because of these weaknesses and the desire to go further into the sectoral relative prices, the next sub-section outlines an alternative approach and presents the results.

1/ See Plon (1984).

2/ The two available CPIs for the Ivory Coast are calculated on the basis of a 1960 consumption basket for Abidjan only, one for middle-income families called the African CPI and the other for high-income families called the European CPI. The latter contains a large import component and parallels the change in import prices compared to the former which contains a larger domestic component, but neither represents the consumption patterns of the rest of the economy.

2. Relative producer prices

Further examination of relative price developments is constrained by the data available. To provide the greatest sectoral richness, the analysis presented below is based on the producer price increases by sector that are reported in the economic budgetting and national accounting data.1/ The sectors have been grouped first, into tradables and non-tradables, where tradables include mainly agricultural and industrial sectors, and non-tradables include energy, construction and services.

The contribution to GDP that is the margin between producer and export prices is a separate category in the analysis. As seen below, this export margin is not insignificant in the analysis. Given some fixed producer prices, it reflects world price and exchange rate movements.

The groups have been divided further into sectors where prices are flexible and those where prices are fixed. The fixed price tradables sectors include most agricultural exports, including coffee and cocoa, oil, palm oil, and rice, where the government sets the price and changes it periodically. For the major exports of coffee and cocoa, for example, the producer price is set well below the world price to generate government revenues, part of which are optimal, given the international coffee quota arrangement and Ivory Coast's large share in the world cocoa market. For rice, the government offers a fixed price at its mills but farmers are free to sell elsewhere. The remainder are considered flexible price. For non-tradables, the energy and communication sub-sectors and import duties and taxes are classified as fixed

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1/ While it would also be useful to analyze the relative prices facing consumers, the absence of disaggregated sectoral consumer price data prevents such an exercise.

price, and the transport sector is classified as a mixture of fixed and flexible price.

During 1981 and 1982, as shown in Table 8, the relative producer price of tradables to non-tradables decreased. While non-tradables prices increased 9.9 percent and 14.7 percent, respectively, tradables prices increased by only 4.5 percent and 5.3 percent, respectively. This relative price trend was evidenced in both the fixed and flexible price area. In the flexible price sectors, one can hypothesize that the tradables prices were guided by external exchange rate and price developments while the non-tradables prices were responding to domestic monetary developments. It appears that the domestic monetary restraint in the early 1980s was not sufficient to encourage the relative price changes at this stage necessary for medium-term adjustment. An important factor contributing to the unresponsiveness of the tradables price was the low level of change in the tradables fixed prices, 3.9 percent in 1981 and 0.1 percent in 1982. This was due mainly to the producer prices facing coffee and cocoa growers. Other agricultural fixed prices kept up with inflation but did not increase sufficiently to alter the relative prices facing producers.

In 1983, the relative price trend reversed slightly, with price increases of 6.5 percent and 14.0 percent for non-tradables and tradables prices, respectively. However, the tradables price increase came primarily from the flexible price sector and, within that, non-exported food products whose production and prices were severely but only temporarily affected by the drought.

It is only in 1984 that one sees the relative price signals of a real depreciation generated in the fixed tradables price sectors. Aggregate fixed agricultural prices increased 9.8 percent, with a steady increase in coffee

and cocoa prices and large increases for other agricultural goods. The lagged effects of the tighter monetary policy and the recession are finally evidenced in the lower inflation of the non-tradables sector, other than hydroelectric power where prices surged because of the drought.

In light of the adverse external developments of 1981-83, the balance of payments position of the Ivory Coast had deteriorated considerably, and unfortunately the relative price of tradables to non-tradables did not reflect this difficulty. It appears that the monetary policy pursued in the early 1980s did not put a sufficient brake on general prices. In addition, fixed tradables prices were not adjusted sufficiently to reflect the new situation. The oligopolistic position of the Ivory Coast in the world coffee and cocoa markets suggests that the government should keep a portion of the rents due to the exchange rate depreciation, but the coffee and cocoa price increases over the period were not sufficient to maintain real prices. The adjustments to prices offered to producers of other agricultural goods were larger, particularly in 1982 and 1984, but did not result in any significant change in the incentives in those tradables sectors. The depreciation of the real exchange rate as reflected in the export-weighted index presented in the previous subsection is due to the massive increases in the export margin, 43 percent in 1982, up to 74 percent in 1984, and does not indicate a change in producer incentives.

IV. Impact of UMOA Policy on Medium-Term Adjustment

A. Implications of Continuation of Existing Process

1. Debt rescheduling

Since 1981, the BCEAO has engaged in monetary restraint complemented by the fiscal restraint of the Ivory Coast government. While there has been relative success in cutting back monetary growth and moderating inflation, the country failed to move toward UMOA's short-term balance of payments equilibrium objectives changes until 1984. That balance of payments result was due to both an export recovery and a debt rescheduling. Again in 1985 debt rescheduling is expected to contribute significantly to a balance of payments equilibrium outcome.1/ As long as the debt rescheduling is sufficient for balance of payments equilibrium in the upcoming year, the UMOA system need go no further in analyzing the medium-term implications of its monetary policy.

The role of debt rescheduling under the existing Paris and London Club frameworks is to alter the time profile of the debt service to relieve a short-term difficulty. The economic adjustment that may be required to service that debt and to restore capital market confidence must still take place. The recent medium-term projections for the Ivory Coast illustrate that the external debt servicing burden remains enormous. 2/ If monetary policy is set each year with debt rescheduling as the fallback, this creates future problems for the monetary union both when interest service continues to rise

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1/ In the context of BCEAO's monetary policy setting process for 1985, public debt principal payments are estimated at a little over CFAF 100 billion compared to CFAF 270 billion due on existing debt as of the end of 1983, three-quarters of which is due to private financial institutions.

2/ See World Bank (1984) and IMF (1984a).

and should external lenders suddenly balk at this process. From the point of view of macroeconomic adjustment, rescheduling is similar to a further drawing down of the Operations Account, with a slight difference in interest rate implications, as long as it is assumed that the Operations Account eventually is to be replenished. The major difference is that the rescheduling of public debt directly eases the fiscal situation whereas the government does not have direct access to the central bank's drawdown on the Operations Account once its statutory borrowing limit has been reached. The BCEAO, on the other hand, is primarily concerned with the Operations Account and reacts quite differently in terms of its monetary policy in the face of a rescheduling. In the event of continuing external debt resecheduling, the monetary authorities may feel less pressure to institute policies promoting further current account adjustment.

2. Prices

As discussed in earlier sections, UMOA's monetary policy takes largely a passive view of inflation. In addition, there is an implicit satisfaction with low levels of inflation near trading partner levels (adjusted for the nominal exchange rate) based on a purchasing power parity concept of the real exchange rate adjustment. Continuing satisfaction with the real effective exchange rate level prevailing in the Ivory Coast does not appear to bring balance of payments equilibrium in the projections. Yet without a real exchange rate change, such equilibrium would only come from unemployed resources in the non-tradables sector. It is more useful to think in terms of the real exchange rate consistent with balance of payments equilibrium and full employment. Because the nominal exchange rate is exogenous, the monetary authorities' impact on the domestic price level and therefore relative prices becomes more crucial.

B. Limitations to Relative Price Adjustment

The previous section suggests that BCEAO should be concerned with and consider the medium-term scenario and relative price developments, in particular. Once considered, there is still the question of what impact the BCEAO could have. If one were willing to ignore a number of rigidities in the Ivory Coast's economy, the BCEAO could be encouraged to reduce the money supply further with the instruments at its disposal, which in the simplest of models would lead to a fall in the non-tradables prices with tradables prices determined in an open economy framework and thus to a real exchange rate depreciation. This section outlines a number of factors that qualify such a recommendation.

1. World inflation and downward price rigidity

One of the phenomena consistently observed in almost all economies in the short run is downward rigidity in nominal prices and wages. For example, in the Ivory Coast, the nominal minimum wage level has remained flat since ----, but a nominal cut would probably be harder to implement despite the lower levels of inflation in 1984-85 than in 1981-82. If one of the objectives were to reduce Ivory Coast wage and price increases to less than those of the rest of the world in order to increase international competitiveness, this task becomes increasingly difficult as world inflation is cut to very low levels. This is the situation currently facing the Ivory Coast. The inflation rates of France and the U.S., two major trading partners, were down to 7.4 percent and 4.5 percent, respectively, in 1984 and are expected to remain low, for example, at 5.4 percent and 5.0 percent, respectively, in 1985. 1/ Since the majority of the Ivorian economy is agricultural and rural where price and wage

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1/ See IMF (1984b).

flexibility is often assumed to prevail, downward price rigidity may be less of a problem for the Ivory Coast than for more urban economies, but nonetheless it remains a consideration.

2. Soundness of the financial system

The Ivory Coast financial system already is suffering from the relatively restrictive credit policies of the BCEAO combined with the negative trends in net external assets. 1/ The liquidity ratio of the economy has fallen from 29.1 percent in 1979 to 26.3 percent in 1983 and estimated 25.6 percent in 1984. 2/ The liquidity crisis is valid for the largest four banks, whose reliance on advances from their parent French banks has weakened because of French credit controls, as well as for the smaller ex-development banks which have very limited recourse to additional government funds. 3/ The recession has put additional pressure on the banks from their clients requiring credit to sustain losses. Because of the structural changes being made in the Ivory Coast economy, there is also a portion of the banks' portfolios whose quality has deteriorated permanently, but this is a necessary loss to the banks' owners and should not be confused with the temporary problems stemming from monetary policy.

The forthcoming banking sector report should offer some insights into the soundness of the financial system. Although it is not inconceivable that the system could survive further monetary tightening, there would be large

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1/ See de Boissieu (1984).

2/ Liquidity ratio is calculated as the ratio of M2 at end of the year to GDP based on the BCEAO definition of money. Using the Fund's private money concept, the ratio falls from 25.3 percent in 1979 to 24.3 percent in 1983 and 22.9 percent in 1984.

3/ See Silva-Lopes (1984) and Allain (1985).

risks of financial instability associated with such a policy. In addition, further credit tightening would make a recovery from the recent recessionary years even more difficult, exacerbating the real and financial sectors' woes.

3. Fiscal policy and openness of the system

The experience of the late 1970s has shown potential gaps in overall macroeconomic management in the context of the currency union. The BCEAO's monetary and credit policy can have a limited impact on the real exchange rate unless it is coordinated with fiscal policy and unless temporary surges in net external capital inflows are avoided. The BCEAO's major instrument for control is through demand for its rediscounting facilities. Even if it devised a non-arbitrary way to control level rather than quality of credit through the prior authorization system, the BCEAO is not enabled to control direct credit which bypasses the Ivory Coast banking system.

4. Key fixed prices

The Ivory Coast's government sets a number of producer and consumer prices in the economy, although less extensively than in many other developing countries. The major fixed producer prices relate to the agricultural export sector, including both products grown in the northern savanna area such as cotton and sugar and those grown in the southern forest such as cocoa and coffee, and, less importantly, palm oil and rubber. The government also offers a fixed price for rice, but its purchases have been limited to about one third of production. In total, these products account for 40 percent of tradables production and close to 20 percent of GDP. On the consumer side, the major fixed prices are wheat, rice purchased by the public sector (including imports) and palm oil which represent a much smaller percent of

total consumption, under 5 percent 1/ The prices of the other major food crops such as yams and cassava are determined in the marketplace.

Certainly monetary policy is limited in affecting these key fixed prices. During the period of high inflation and franc depreciation many of these fixed prices were not fully adjusted. If part of the lack of adjustment was due to terms of trade deterioration, that only strengthens the case for relative price change and the need for tradables price changes not to fall behind those of non-tradables. Now, with lower rates of inflation, the lags in adjustment are less damaging. However, any strategy for medium-term adjustment needs to be complemented with an agricultural pricing policy that recognizes the importance of higher relative tradables price increases. Although the correct pricing policy (fixed vs. flexible, degree of taxation) depends on the individual product, market prices on all tradables should have an increase reflecting the medium-term adjustment necessary in the real exchange rate.

It is important to note that such a set of price adjustments by the Ivory Coast's government needs to be accompanied by a non-accommodating monetary policy. If the BCEAO allows these price adjustments to increase the expected inflation variable used in its monetary policy setting process, then monetary growth could increase and offset some of the improvement in the real exchange rate.

1/ The group of fixed prices in the non-tradables sector includes mainly utilities. Any public policy that attempts to keep these prices artificially low runs into fiscal and other problems, and therefore adjustments in those sectors continue to be seen in this light.

C. Conclusions

As emphasized in the preceding sections, the focus of UMOA in setting its monetary and credit policy is the balance of payments position of the Ivory Coast in the coming year. The balance of payments situation as it evolves in the medium-term will become a concern of the BCEAO, but is not taken into account systematically. If the existing process for setting monetary policy continues, only repeated external debt rescheduling can be relied upon in the next few years, with no further attention on the part of the monetary authorities to the evolution of relative price signals which could ameliorate the difficult situation in the medium-term by increasing competitiveness.

Yet the BCEAO acting alone would have difficulty in lowering the overall relative price level. Its major trading partners are also reducing inflation rates; the financial system already faces liquidity problems; certain select borrowers in the Ivory Coast public and private sectors could react to a deflationary policy by external borrowing which would offset the domestic credit efforts; and finally, key agricultural tradables prices are fixed and do not immediately reflect change in external conditions.

What are the alternatives to a deflationary policy, given its limitations and recessionary costs? Certainly the Ivory Coast government's continuing efforts to bring fiscal policy under control reduce the upward pressure on the real exchange rate and allow the productive sectors to respond to those relative price changes.

Second, the Ivory Coast government made a number of upward adjustments in the fixed agricultural prices in 1984, and such efforts should continue. The fixed tradables prices were a major factor in preventing a change in relative price signals until 1984. This includes raising prices of

not only export crops but also other tradable agricultural products which may be primarily domestically consumed or imported (e.g., wheat) where the price increases on the latter can offset some of the negative revenue aspects of the former. The government may also wish to consider introducing processes for increasing the flexibility in price formation to prevent deterioration in price signals in the medium term. However, it is important to note the interrelationship between the government's price policies and the central bank's monetary policy. For the government policy of altering fixed agricultural prices to be successful in sending appropriate signals, the BCEAO would have to continue a degree of monetary restraint to ensure that its policies did not simply accommodate the price increases.

Third, tariff-cum-subsidy schemes could be introduced to the trade accounts. The Ivory Coast's government introduced a scheme for the industrial sector in 1985 with approximately revenue neutral implications. If extended to the entire economy, such schemes raise the price of tradables, with a tariff on imports and a subsidy on exports. Again, for the commercial policy to affect relative prices, monetary restraint would have to continue so as to continue downward pressure on prices in other sectors of the economy, and not to accomodate those price increases. The scheme has shortcomings, although not necessarily critical ones. One is that the scheme drives wedges between various categories of transactions. Without being extended to the transactions of the services account, the scheme can be distortionary to the extent that the degree of substitution between goods and services is high, which does not appear to be the case for the Ivory Coast. On the capital account side, the shortcomings are similar to those of a dual exchange rate system, especially if transactions can leak easily between accounts. Other problems of instability of the capital account in dual systems would not occur since

the expected rate of depreciation in both markets would be the same. The objective of the adjustment process is not balance of payments equilibrium but economic growth consistent with certain constraints placed on the performance of the Ivory Coast's balance of payments. Therefore, as alternatives to a painful deflationary policy, each of these options deserves further exploration.

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Table 1: BCEAO INTEREST RATE STRUCTURE

	Effective Date					
	Before 01-29-73	01-29-73	07-01-75	04-14-80	04-07-83	04-05-83
Rediscount Rate	3.5	5.5	8.0	10.5	12.5	10.5
	End of Period					
		79	80	81	82	83
Ivory Coast						
Rediscount		8.0	10.5	10.5	12.5	10.5
Interbank money market rate /a		10.0	10.1	14.6	13.3	12.3 /b
France						
Bank of France discount rate		9.5	9.5	9.5	9.5	9.5
French interbank money market rate		9.5	12.2	15.3	14.7	12.6

/a Rates quoted are for overnight advances.

/b Quoted rate for June 1983.

Sources: BCEAO, IFS.

Table 2: EXCHANGE RATE INDICES, IVORY COAST, 1970-1983 /a

(1980=100)

	70	75	79	80	81	82	83
Deflated by CPI /b							
Export weighted							
Nominal	104.3	98.2	100.6	100.0	103.8	110.6	115.7
Real	129.3	130.6	102.3	100.0	106.4	116.1	123.2
Import weighted							
Nominal	103.2	97.6	100.5	100.0	106.0	111.1	116.1
Real	129.5	130.0	101.4	100.0	109.3	117.6	125.2
France							
Nominal	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Real	81.3	74.2	99.2	100.0	96.0	92.1	89.0
Deflated by GDP deflator							
Export weighted							
Nominal	98.2	100.6	100.0	103.8	110.6	115.7	
Real	116.5	98.1	100.0	110.0	115.6	116.8	
Import weighted							
Nominal	97.6	100.5	100.0	106.0	111.1	116.1	
Real	116.5	97.3	100.0	112.6	115.9	117.0	
France							
Nominal	100.0	100.0	100.0	100.0	100.0	100.0	
Real	84.8	103.3	100.0	93.1	92.4	93.8	

a/ Average exchange rates during the period.

b/ Deflated by trading partners' CPI and Ivory Coast's Abidjan (African)CPI.

Source: IFS.

Table 3: MONETARY SUMMARY, IVORY COAST, 1980 - 1984

	Billions of CFAF					% Annual change						
	80	81	82	83	Proj. End 84	80	81	82	83	Proj. 84	80-83	Proj. 80-84
Net foreign assets	-243.7	-389.5	-432.6	-634.3	-668.7	-253.2	-59.8	-11.1	-46.6	-5.4	-34.6	-28.5
Central Bank	-126.9	-279.9	-328.2	-494.9		-1,203.5	-120.6	-17.3	-50.8		-52.8	
Banks	-116.8	-109.6	-104.4	-139.4		-45.1	6.2	4.7	-33.5		-4.9	
Domestic credit	835.0	1,028.0	1,098.2	1,314.5	1,391.7	23.2	23.1	6.8	19.7	5.9	15.3	13.5
Government	-54.7	61.5	77.0	213.8		108.4	212.4	25.2	177.7		109.2	
Other	889.7	966.5	1,021.2	1,100.7		12.4	8.6	5.7	7.8		7.2	
- Ordinary credit	763.6	779.3	848.7	937.1		9.0	2.1	8.9	10.4		7.2	
- Agric. credit	126.1	187.2	172.5	163.6		38.6	48.5	-7.9	-5.2		7.2	
(Refinanced by BCEAO)	(271.9)	(372.3)	(412.1)	(474.7)		33.2	36.9	10.7	15.2		19.4	
Money supply	581.8	639.7	660.3	695.4	730.0	2.8	10.0	3.2	5.3	5.0	5.8	
Base	438.7	464.4	460.3	489.6		1.1	5.9	-0.9	6.4		3.3	
Other items (net)	9.6	-1.5	5.3	-15.1	-7.0							
Private money concept used by the IMF:/a												
Net domestic assets	754.6	940.4	1,004.7	1,222.1	1,262.0	40.9	24.6	6.8	21.6	3.3	16.3	13.8
Net claims on public sector	-6.6	96.7	118.9	260.0		94.6	1,565.2	23.0	118.7		219.4	
Net claims on private sector	761.2	843.8	885.9	962.1		15.6	10.9	5.0	8.6		7.8	
Private money and quasi money /b	537.5	579.1	609.1	644.7	652.0	9.1	7.7	5.2	5.8	1.1	6.1	5.1

/a Domestic credit less medium and long term foreign liabilities of the banks, bank deposits of industrial and commerical public agencies (EPIC's) and of state enterprises (SODEs) and other items (net).

/b Money and quasi money less bank deposits of EPICs and SODEs.

Sources: For 1980-83 figures, BCEAO, Statistiques Economiques et Monetaires; for 1984 projections: BCEAO, Abidjan.
For item used by the IMF: IMF staff estimates.

Table 4: BALANCE OF PAYMENTS SUMMARY, IVORY COAST, 1981 - 1984

(billion CFAF)

	81	82	83*	84**
Exports	743	806	797	1,078
Imports	-560	-607	-574	-602
Trade Balance	183	199	223	476
Services	-369	-409	-435	-523
(interest on public debt)	(-102)	(-162)	(-198)	(-263)
Transfers	-135	-147	-132	-129
Current Account Balance	-321	-357	-344	-176
(percent of GDP)	(13.8)	(14.3)	(12.7)	(6.1)
Capital Inflows	350	518	342	343
Outflows	-177	-212	-258	-111
Capital Account Balance	173	306	84	232
Balance	-140	-51	-179	-40

Source: BCEAO

* provisional
** estimated

Table 5: USE OF REDISCOUNT FACILITIES, IVORY COAST, 1979 - 1984

(billions CFAF, end of period)

	79	80	81	82	83	July 84 /a
Credit to Private Sector	792	890	967	1,021	1,101	1,009
Of which financed by central bank	(204)	(272)	(372)	(412)	(475)	(370)
Percent rediscounted including seasonal agricultural credit	26	31	39	40	41	37
Percent of ordinary credit rediscounted /b	16	19	24	28	33	23

/a Latest available at BCEAO. Because of seasonal fluctuations, the July figure tends to be a few percentage points lower. At the end of July 1983, only 37% also was rediscounted.

/b Assuming all seasonal agricultural credit is rediscounted.

Source: BCEAO, Statistiques Economiques et Monetaires.

Table 6: COMPARISON OF REQUESTS AND PRIOR AUTHORIZATIONS GRANTED, IVORY COAST, 1981 - 1984

(percentage)

	81	82	83	84
Total Granted/Requests	79	92	47	83
Primary sector and agricultural seasonal credit	74	89	17	73
Industrial sector	88	95	97	98
Tertiary sector (excluding agricultural credit)	95	96	96	95
Other sectors	95	95	95	99

Source: BCEAO, Abidjan.

Table 7: CONSUMER PRICE CHANGES AND MONETARY GROWTH, IVORY COAST 1980-1984

(Percent)

	80	81	82	83	84
Money supply/a					
BCEAO definition	2.8	10.0	3.2	5.3	5.0
IMF definition	9.1	7.7	5.2	5.8	1.1
CPI (1980 = 100)					
African	12.8	8.8	8.0	6.9	
European	8.0	13.2	14.3	7.8	

/a See Table 3.

Table 8: PRODUCER PRICE CHANGES, IVORY COAST, 1981-85

(percentage change)

Sector /a	81	82	83	84	Proj. 85
Total /b	5.8	12.6	12.7	14.3	5.5
Nontradables /c	9.9	14.7	6.5	7.4	5.7
Tradables /c	4.5	5.3	14.0	7.1	7.5
Export margin /c	-35.3	42.9	49.6	74.1	-4.6
Nontradables					
Fixed price	10.7	18.3	9.0	11.7	7.7
Flexible price	8.3	13.4	5.3	5.8	4.9
Mixed	15.0	12.0	6.2	5.2	5.6
Tradables					
Fixed price	3.9	0.1	5.6	9.2	2.2
(i) crude oil	26.2	4.7	6.0	8.9	4.8
(ii) coffee & cocoa	0.7	-7.0	6.8	7.0	0.3
(iii) other agricultural	6.6	17.8	3.4	12.6	3.4
Flexible price	4.8	8.2	18.7	6.2	11.0

/a The following 4-digit classification of sectors was used:

Nontradables: fixed price--5200-6999
flexible price--7100-7299, 7400-9999
mixed--7000-7099

Tradables: fixed price--0110, 0200-1999, 2006
flexible price--0100-0199 except 0110, 2000-4999 except 2006

Export margin: 7300-7399

/b GDP price deflator weighted by valued-added of sectors.

/c Weighted by total value of production of sectors. Total price percentage changes using this method for 1981-85 are: 5.8, 12.6, 12.7, 14.3, 5.5.

Source: Budget Economique