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Guinea: Ex Post Assessment of Longer-Term Program Engagement

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GUINEA

Ex-Post Assessment of Longer-Term Program Engagement

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I. Introduction

1. Notwithstanding its rich endowment in natural resources, Guinea remains one of the poorest countries in the world, with per capita GNP estimated at US$400 in 2002. Guinea is a large and sparsely populated country, of which the majority of the population of about 8.5 million is engaged in agriculture. However, the country has also considerable natural resources in mining, especially bauxite, iron, and precious metals. Following independence, Guinea introduced an economy based on strict presidential control, with restricted private sector activity. A new regime started a broad range of market-oriented economic reforms in the late 1980s. However, while the country made good progress on stabilizing the economy and consolidating the transition to a market economy during 1987–96, performance has weakened since then.

2. **Guinea's political system has been based on a single-party presidential regime with serious restrictions on opposing views**. During the 1990s, some political freedom was allowed. However, presidential elections in 2003 were deemed to have been deeply flawed and political uncertainty is increasing because of the president's failing health and divisions in the ruling party. In addition, the resumption of the civil war in Sierra Leone in 1999 and the armed conflicts in Liberia and Côte d'Ivoire have caused serious security concerns.

3. Regional insecurity has imposed a toll on economic activity and on the budget. The continued presence of almost 750,000 refugees—from Sierra Leone, Liberia, and Côte d'Ivoire—adversely affected social and economic infrastructure and disrupted economic activity in the relevant border areas. Moreover, Guinea participated in peace keeping missions in neighboring countries, straining its limited resources. Furthermore, sporadic rebel incursions into Guinean territory led to increased defense spending to preserve the country's territorial integrity.

4. **Guinea's stabilization and reform efforts have been almost continuously supported by Fund financial arrangements since 1987 (Table 1)**. This paper reviews developments under the last two Fund-supported programs during 1997–2004 and is organized as follows: Section II discusses program objectives, policies and performance and Section III reflects on lessons learned and the remaining challenges. Section IV concludes with a discussion on possible future relations between the Fund and Guinea.

II. Engagement with the Fund, 1997 to Present: Program Objectives, Policies and Performance

A. Program Objectives and Policies

5. **Guinea made considerable progress under its economic programs supported under ESAF-arrangements from 1991, but fiscal management deteriorated by 1995–96.** Growth averaged almost 4 percent per year and inflation declined from almost 20 percent in 1990 to 3 percent by 1996. However, the external situation did not improve as much as expected because of a sharp deterioration in the terms of trade as international prices for

bauxite and aluminum declined, resulting in a 7½ percent of GDP fall in government revenue from this sector. The situation was aggravated by a slackening in government finance management in 1995–96. By end-1996, international reserve coverage had fallen to 2 months of imports and the Central Bank suspended a high level of transfers abroad.

6. **Guinea implemented important structural reforms during this period, but much remained to be done**. These reforms concerned a legal framework for privatization, central bank and banking acts, a mining code, tax reforms (including the introduction of a VAT), the liberalization of external current account transactions, and the introduction of an interbank foreign exchange market and of market-based monetary policy instruments. However, development of the private sector proceeded slowly, because of an unreliable and non-transparent administrative and judicial environment, the poor condition of physical infrastructure, the fragile state of the banking system, and to some extent political uncertainty and insecurity in areas bordering countries in conflict.

7. **Against the background of fiscal difficulties and stagnant private sector development, the main objectives of Guinea's medium-term programs supported by Fund arrangements during 1997–2004 have been to reduce financial imbalances and promote sustainable private sector-led growth.** The growth objectives were predicated on greater fiscal discipline and an improved quality of public investment, accompanied by crucial reforms in the financial and judicial systems. These, together with sectoral policies in agriculture, mining, fisheries, and trade, were expected to contribute to removing obstacles to private investment. Fiscal programs under different arrangements aimed at continued consolidation and a gradual shift in allocations to the social sectors and from wages to nonwage outlays.

8. **Monetary policies aimed at containing inflation and at reaching a prudent level of international reserves** by maintaining tight domestic liquidity conditions through a variety of channels, including active use of open market operations, strict enforcement of minimum reserve requirements, observing quarterly ceilings on reserve money and targets for net foreign assets of the central bank, and raising the interest rate on central bank credit to the government to the level of the treasury bill rate. In addition, a more flexible exchange rate policy based on foreign exchange auctions was to be introduced.

9. **Financial sector policies were aimed at restoring the health of the banking system.** Weak banks were to be restructured and supervision strengthened, including by applying the Basel Core Principles in assessing commercial banks' balance sheets. More recently, in the context of the Poverty Reduction Strategy Paper (PRSP), the financial sector development strategy assigned considerable importance to financial services to small and medium-sized economic agents through microfinance institutions (MFIs).

10. **External sector policies aimed at improving the competitiveness of exports, achieving the sustainability of external debt, and accumulating adequate international reserves as a cushion against shocks.** The authorities have also aimed at promoting trade

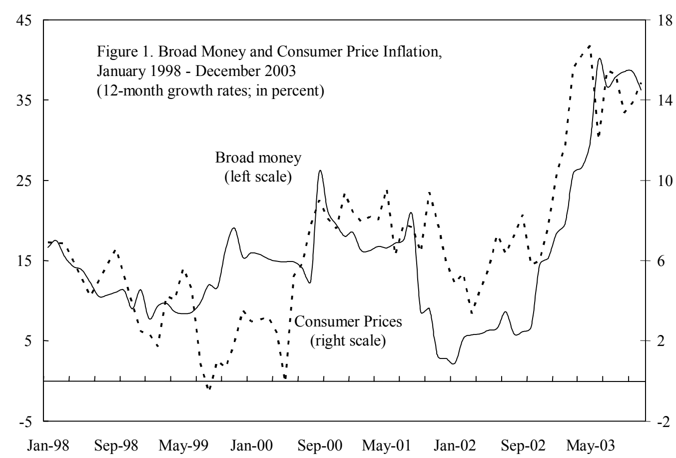
through simplified customs procedures and the removal of restrictions on current payments and transfers.

11. **Structural reform targeted reducing the size of the public sector, while increasing efficiency and the quality of public services.** In addition to a reduction in the large civil service, the objectives included judicial reforms and promotion of better governance, and measures to strengthen the fishing, mining, and energy sectors (Table 2).

12. **Social policies under the programs focused on reducing poverty through improving the delivery of basic social services, such as health, education, and safe drinking water**. The poverty reduction effort was intended to be boosted by resources made available through debt relief under the Enhanced Initiative for Heavily Indebted Poor Countries (HIPC) Initiative.

B. Performance Under Fund-Supported Programs

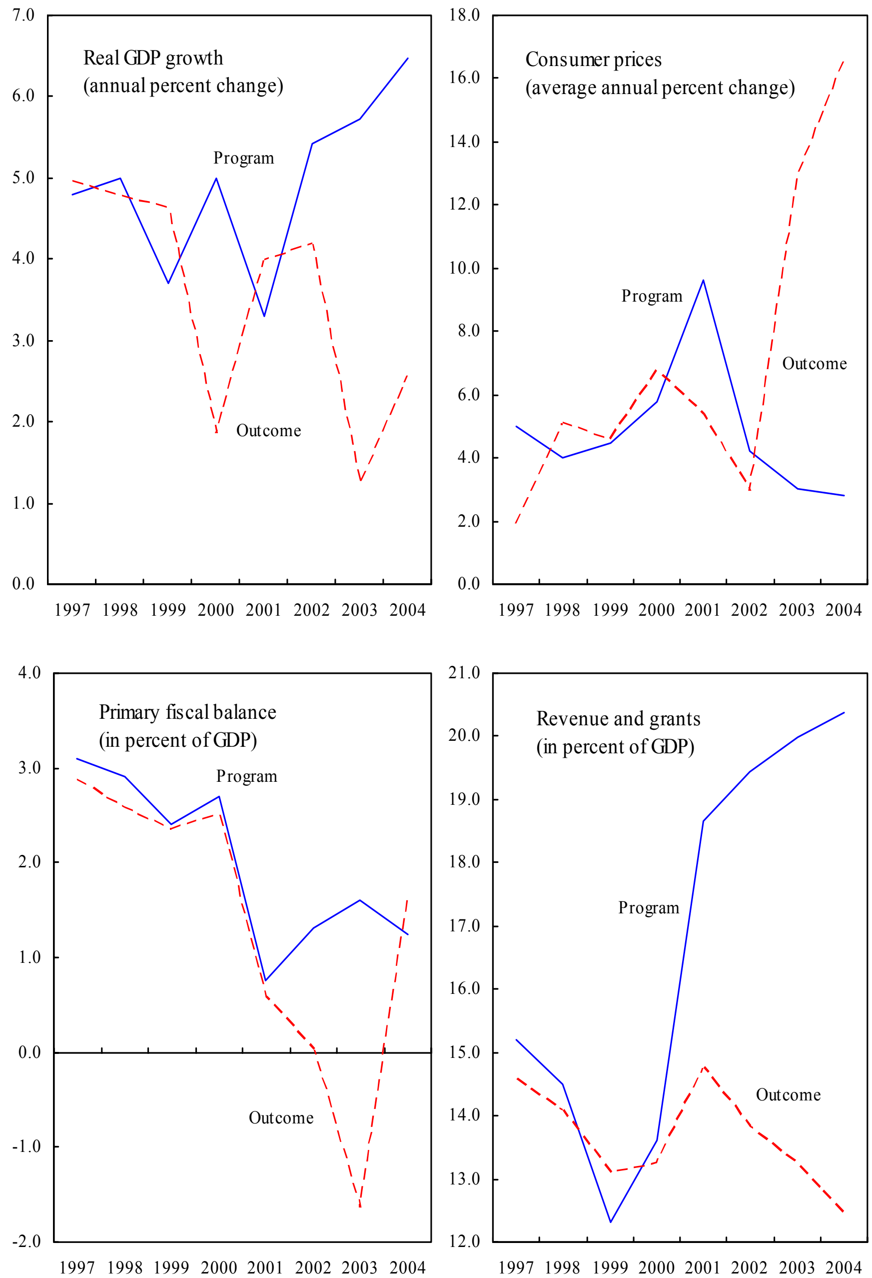
13. **Performance under the two most recent Fund-supported programs has been disappointing** (Figures 1 & 2). Economic growth initially increased as intended to an average of 4.5 percent during 1997–99, but declined to below the average of the early 1990s thereafter compared to a strong increase projected under the program. Initially, the authorities were able to keep inflation under control by tightening monetary policies to contain inflationary pressures during periods of fiscal slippages. However, in the past two years, monetary policy accommodated the expansionary fiscal stance, and inflation accelerated to double digits. On the external side, international reserves' coverage remained slightly below target in the first years under the program, but fell from 3.1 months of imports in 1998 to 1.5 months by 2003. Finally, progress in implementing structural reforms was weak.



Public finances

14. **Performance in the fiscal area has been erratic and intervals of satisfactory progress were mixed with periods of noncompliance with program targets, reflecting both revenue shortfalls and expenditure overruns.** Revenue from the mining sector declined by about 1½ percent of GDP during 1997–2003, in line with the continued fall in international prices. Nonmining revenue consistently remained below the program targets,

Figure 2. Guinea: Real Sector Indicators and Financial Operations of the Government: Program Targets and Outcomes, 1997 - 2004



Sources: Guinean authorities; and staff estimates and projections.

especially since 2000. Current expenditure exceeded the targets in virtually every year during the period under review; the excess was 1 percent of GDP or more in 2002 and 2003, especially owing to higher defense expenditure in response to a further deterioration in the regional security situation. Reflecting ad hoc cuts in capital expenditure, the fiscal primary balance remained on target until 2001, but declined from a surplus of 2.6 percent of GDP on average during 1997–2000 to a deficit of 1.6 percent of GDP in 2003.

15. **Revenue mobilization has been weak, with major shortcomings in tax administration, widespread corruption, and extensive use of tax and customs exemptions.** Moreover, lack of progress on two key issues has adversely affected fiscal consolidation. First, Guinea has been unable to make the effective transition from dependence on large mining royalties that fell in line with the structural decline in bauxite prices.[2] Two, delays in restructuring public enterprises, in particular the key public utilities (telecommunication, electricity, and water), have also compromised revenue targets. While Fund programs recognized these problems and proposed measures to address them, they were only partially successful as political opposition prevailed.

16. **Measures to address shortfalls have often failed to address the real cause of the problems, and were aimed only at attaining program targets to complete reviews.** Such actions have included ad hoc revenue measures, postponement of, or unsustainable cuts in, expenditures until after measurement dates,[3] and unconventional budgetary and accounting procedures, as well as higher bank financing. Such measures led on several occasions to delays in completing reviews or, as was the case in early 1999 and 2001, resulted in new programs going off-track quickly after their approval.

17. **On the positive side, Guinea made progress in increasing spending to education and health.** Spending for these sectors more than doubled during 1997–2002. However, the levels are still below the average for sub-Saharan Africa, and believed to be insufficient to

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[2] Nonmining revenue rose by only a paltry 0.5 percent of GDP over 1997–2003 to 9 percent of GDP in 2003.With mining revenue falling from 3 percent of GDP in 1997 to 1.5 percent of GDP in 2003, the total revenue-to-GDP ratio decreased by 1 percentage point over the same period to 10½ percent of GDP.

[3] For example, to observe the March 1997 criterion, normal expenditure procedures were suspended and replaced by a stringent control of cash outlays by a top-level Cash Management Committee, which cut all expenditure without prioritization, including in the social sectors. This situation repeated itself in 2000-01, when revenue shortfalls, coupled with overruns in defense spending, led to ad hoc revenue mobilization measures and to draconian expenditure compression that enabled the authorities to the meet primary balance performance criterion for end September 2001 and end-March 2002, respectively.

achieve the Millennium Development Goals.[4] The 2003 public expenditure review (PER) recommended that actions be taken to complete the costing and prioritization of poverty reduction programs, so as to better target budgetary allocation toward and within social sectors and to improve the tracking of expenditure.

Monetary and financial sector

18. **Monetary policy implementation has been uneven.** At times, it has accommodated poor fiscal performance, resulting in breaching monetary targets. At other times, there has been a short-lived attempt to become more proactive. As a result of the lack of independence of the central bank and monetary policy, the targets have been missed on many occasions; the floor on net foreign assets has been missed almost continuously since 1997. From 2001 onward, and in particular since mid-2002, monetary policy accommodated fiscal expansion, which largely reflected high security spending.

19. **Monetary management benefited from an increased use of indirect instruments, but this did not contribute to effective liquidity management.** Auction mechanisms for central bank bills and treasury bills were introduced, but their effectiveness was compromised either by lack of effective coordination with fiscal policy or by the continuation of fiscal dominance. The conduct of monetary policy was also affected by structural factors, such as the cash nature of the economy (the currency-to-broad money ratio averaged over 46 percent during 1997–2003), which impeded the functioning of proper credit channels.

External sector

20. **Developments in the external sector also remained below expectations.** Much lower prices for mining products caused an average annual shortfall in export receipts of almost 2.5 percent of GDP (Figure 3, Table 3). Lower than projected imports were more than offset by lower grants and other items, and the current account deficit (including grants) exceeded the annual targets by about 3 percent of GDP on average during 1997–2003. International reserves coverage remained slightly below target in the first years under the program, but fell from 3.1 months of imports in 1998 to 1.5 months by 2003.

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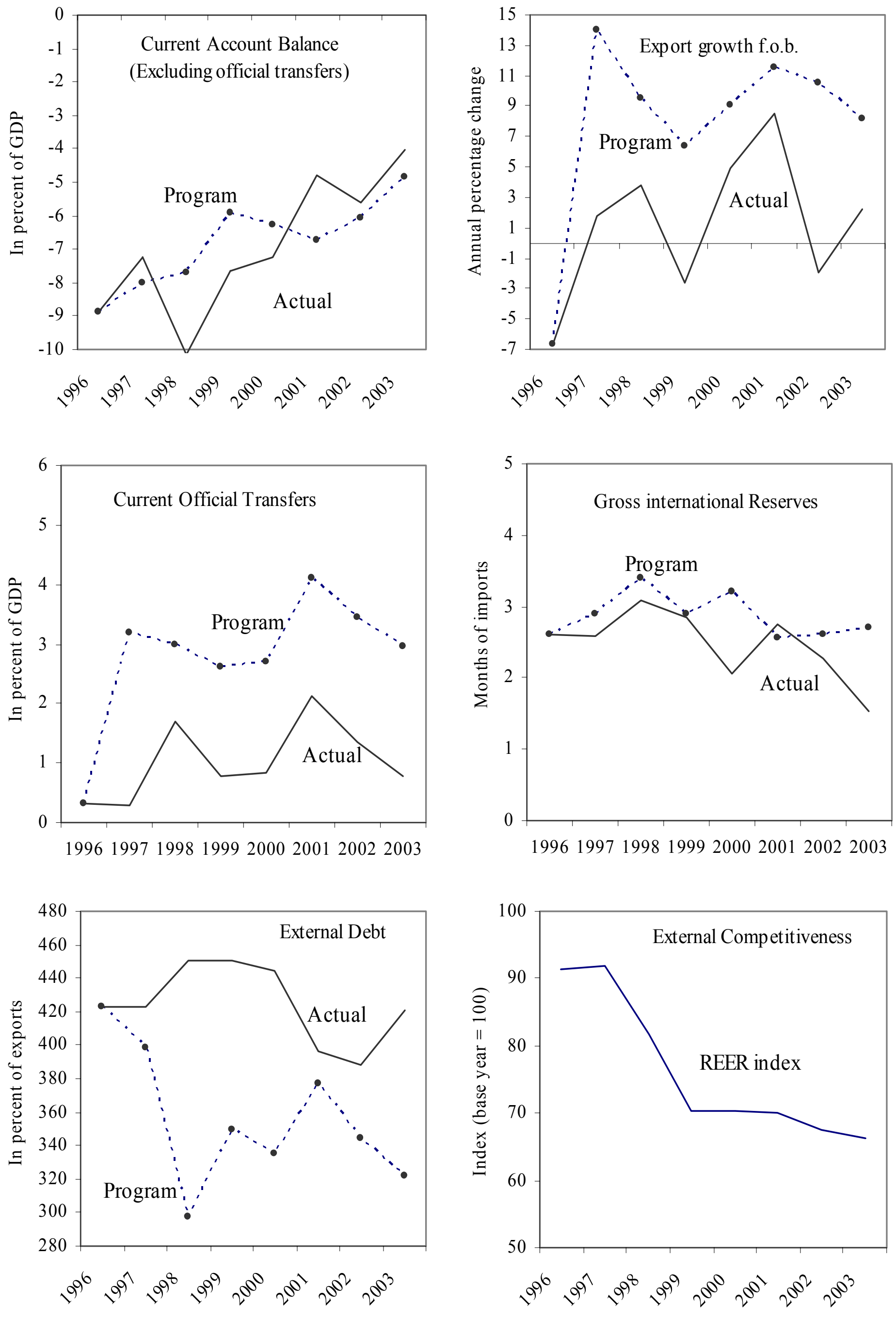
[4] Public spending (current and development) on education and health in Guinea over the period 1998–2001 averaged 2.6 percent of GDP and 1.3 percent of GDP, respectively, compared with an average of 3.4 percent and 2.6 percent, respectively, in sub-Saharan Africa (2003 public expenditure review).

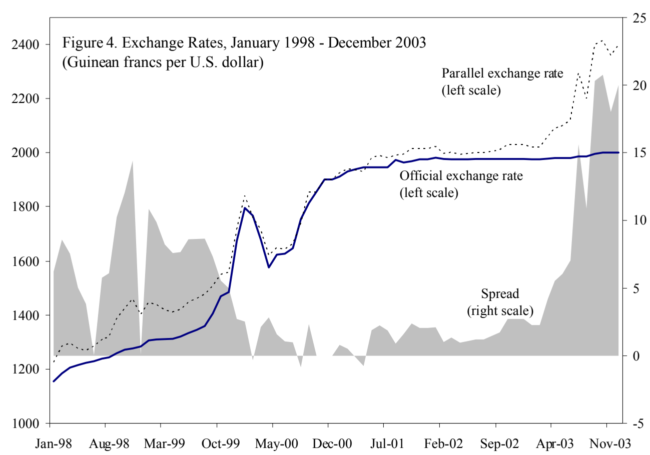
Figure 3. Guinea: External Sector Indicators: Program Targets and Outcomes, 1996–2003



Source: Various staff reports for Guinea.

21. **Guinea gradually adopted a more flexible exchange regime over the past decade but the failure to implement complementary reforms led to the continuation of a strong parallel market**. Improvements in the exchange system included introducing foreign exchange auctions in 1999 and allowing exchange bureaus to participate in the formal foreign exchange market. Moreover, the determination of the official rate generally followed the parallel rate, and, as a result, the spread between the parallel and the official rates remained within a narrow margin. The real effective exchange rate moved around a trend of moderate depreciation, which helped offset to some extent the adverse effects of the weakened terms of trade and shortfalls in foreign aid. However, reflecting the prevalence of cash in financial transactions and the existence of informal channels for international transfers, the government was not successful in integrating the parallel market into the formal foreign exchange market and an estimated 70 percent of the foreign exchange transactions continued to be channeled through the parallel market.

22. **Reflecting the decline in mining receipts and fearing a continued depreciation of the currency, the government reduced the flexibility of the exchange rate again from 2002 onward**. The authorities de facto pegged the official rate against the U.S. dollar, and, starting in the second half of 2003, the foreign exchange auctions became an administrative allocation of foreign exchange to finance priority imports at a predetermined fixed exchange rate. As a result, the spread between the official and the parallel rate widened from around 2 percent in the first half of 2002 to over 20 percent in the second half of 2003 (Figure 4).



23. **Guinea has made progress in liberalizing its trade regime.** Its average import duty of 19 percent remains significantly higher than the average of 12 percent under the common external tariff (CET) of the West African Economic and Monetary Union (WAEMU) member countries but its lower nontariff barriers result in a slightly lower trade-restrictiveness index.[5]

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[5] On a scale of 0-10, where 10 represents the most restrictive trade regime, Guinea and WAEMU countries score 3 and 3.5, respectively. Adopting the WAEMU's CET (planned for 2005) would lower Guinea's trade restrictiveness index to 2.

24. **The liberalization of the trade system and the depreciation of the real effective exchange rate have failed to boost Guinea's trade.** During the past decade, efforts to support the diversification of the economy away from the mining sector have been inadequate. As a result, nonmining exports have been contracting constantly since 1997. To make its exports more competitive, Guinea needs to reduce remaining cumbersome customs procedures, improve institutions, and upgrade its physical infrastructure, all of which were part of the structural reforms under most Fund-supported programs.

External debt

25. **Guinea has also made less progress under the HIPC Initiative than anticipated.** It reached the decision point under the Enhanced HIPC Initiative in December 2000. However, because of poor performance under the PRGF, interim relief by the Fund and the Paris Club stopped after mid-2003 and attainment of the completion point, initially expected to be achieved by end-December 2002, has been delayed at least until 2005. Thus, the external debt service burden remains heavy, which has led to delays in repaying the Fund and the accumulation of arrears vis-à-vis other creditors.[6]

Structural reforms

26. **Many important structural reforms remain incomplete.** In the fiscal area, progress with improving tax and customs administration and strengthening mechanisms for expenditure control has been haphazard. The authorities made good progress in reducing the size of the civil service, resulting in a decline of the wage bill as a share of revenue from almost 44 percent to 34 percent during 1996–2003.[7] However, implementation of reforms aimed at making civil servants more efficient by introducing a merit-based promotion and remuneration system has stalled. The number of state-owned enterprises (SOEs) was reduced from almost 240 in the 1980s to only about 70 by 2001. In more recent years, the privatization efforts slowed down because the authorities were dissatisfied that the first wave of privatizations did not yield the expected increase in production and employment. Due also to the absence of political will to tackle outstanding fundamental issues, the important

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[6] Since 1997, Guinea has incurred late payments to the Fund on 20 occasions. Recently, with the deterioration in the economic situation and financial difficulties in meeting external obligations, the payment record worsened, with four late payments already in 2004. However, Guinea made efforts to repay the Fund ahead of all other creditors.

[7] Most of the reduction was done under the first arrangement of the 1997–2001 ESAF. Since then, the reduction has been of only about 2 percentage points. The 2003 World Bank PER indicated that efforts were needed to continue shifting resources from wages to nonwage outlays, including in the social sectors.

restructuring and privatization of the public utilities has been delayed, imposing a toll on private sector development.

27. **Progress with improving the health of the financial sector has been very good and financial indicators suggest that the banking sector has remained relatively sound**. Bank restructuring advanced, supervision improved, including of MFIs, and important steps have been taken to improve financial sector regulations. Capital adequacy and liquidity ratios are broadly in line with prudential levels. The level of nonperforming loans remains quite high (above 25 percent), although provisioning has been increased (to 89 percent of nonperforming loans). On a negative note, the measures recommended as critical by a Fund's safeguards assessment mission in May 2002 have not yet been implemented. Also, while financial reforms have helped in improving the soundness of the banking sector, they have not been sufficient to make it a reliable source of finance for private sector development. Further measures to this extent would have to include strengthening of the judiciary—with the assistance of the World Bank—for better loan recovery, including through seizure of collateral assets.

28. **Key reforms in other areas have generally not been implemented** (Table 2). As a result, corruption remains widespread, and the legal system weak.[8] Electricity production is still unreliable and virtually none of the measures to strengthen specific economic sectors has been implemented. A study conducted in the context of the Integrated Framework in 2002/03 highlighted the many remaining structural problems hampering trade that had already been identified in previous years.

C. Involvement of—and Fund Relations with—Other Donors

29. **Many donors were involved in providing financing and technical assistance during 1997–2004.** The World Bank has been the primary provider of concessional financial assistance, accounting for almost 25 percent of Guinea's official development assistance, followed by the AfDB Group and the European Commission. However, mainly because of weak performance, a large share of the committed assistance has not been disbursed. In addition, donors have provided extensive technical assistance, some of which was in close collaboration with, and complementary to, assistance provided by the Fund. Nonetheless, there were weaknesses in coordination prior to the PRSP era.

30. **Coordination among donor agencies improved starting with the 2001–2004 PRGF-supported program, in particular between the Fund and the World Bank.** The resulting clearer division of labor allowed structural conditionality in Fund-supported

[8] In 1997, the World Bank country assistance strategy had a judicial capacity building program in the base case scenario. However, it was dropped because Guinea moved to the low case scenario and because of lack of commitment from the authorities.

programs to be streamlined and limited to the Fund's core areas of expertise; the number of structural performance criteria/benchmarks dropped from an annual average of 15 during 1997–2000 to 5 during 2001–02.[9]

D. Implementation of Fund-Supported Programs

Commitment and ownership

31. **Despite close to two decades of IMF-supported adjustment and reform programs, Guinea has not yet been able to sustain consistent implementation of a long-term development strategy**. A lack of ownership of the programs at the highest level of government,[10] powerful vested interests wary of reforms that threatened their rents, and significant governance problems, have slowed down the implementation of policy measures that had the potential of benefiting the population at large. Accordingly, after Guinea made considerable progress in laying the basis for a market-based and private-sector led economy, implementation of key measures aimed at unlocking Guinea's growth potential stalled and the reform agenda remains largely unfinished. In this context, performance under Fund-supported programs during 1997–2004 was similar to previous periods: some progress followed by periods of regression with the overall implementation remaining feeble. As a result, economic growth remained well under the potential of a well-endowed country as Guinea, and the programs' main objectives—a reduction in financial imbalances and sustainable, higher private-sector-led growth—have not been attained.

32. **Attempts to reduce financial imbalances were affected by an adverse external environment, but much of the disappointing results had to be attributed to weak implementation of the reform agenda**.[11] In general, the authorities were complacent in the

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[9] However, the Independent Evaluation Office argued that the Fund's withdrawal from conditionality perceived to be responsibility of the World Bank has not been helpful in all cases. For example, public enterprise reform, while in the Bank's area of competence, was critical for the PRGF-supported program. However, in practice, the different approaches to conditionality of the two institutions made it hard to coordinate effectively, even though there was broad agreement on the objectives.

[10] Guinea's political system consists of a strong presidential regime closely related to the army and lacks checks and balances as the opposition is weak and fragmented. Thus the commitment of the heads of the economic team directly involved in the negotiations with the Fund has often lacked support at the highest level of the government.

[11] Guinea was also confronted with serious adverse external shocks during 1997–2004, namely the fall in the world prices of aluminum and the rebel attacks and influxes of refugees from neighboring countries, which continued to be a major burden on the country, negatively affecting private sector activity and budget execution.

face of the shocks and generally failed to implement compensating measures, except for ad hoc cuts in outlays to meet program targets. For example, the revenue shortfall from the mining sector could have been offset to a large extent by improving tax administration, curtailing tax and customs exemptions, tackling corruption, and improving the investment climate for mining companies. Also, only half of the expenditure overruns in 2002 was the result of additional defense expenditure. More generally, the failure to reach the programs' target of higher economic growth is largely attributable to unfinished key reforms,[12] notably the lack of implementation of measures to reform public utilities and to increase the contribution of fisheries to exports and government revenues. The resulting perpetuation of a weak investment climate—including corruption, weak legal protection, unreliable public service, lack of financial services—has discouraged new investment that would have increased growth, diversified exports, and bolstered government revenue, reducing the country's vulnerability to such shocks.

33. **The sluggish implementation of reforms also partly reflects weak capacity.** Capacity remains low in line with Guinea's low level of development and despite considerable technical assistance. Nonetheless, yet again, program policies in many areas could not be implemented because of insufficient political support. Examples are the regular bypassing of existing control systems, the many attempts to hide problems temporarily in order to complete program reviews, the lack of progress with the reform agenda once it encountered stronger vested interests, and despite good advances during some periods, the abandonment of financial stability if politically expedient, such as during the end-2002 and 2003 pre-electoral period.

34. **With doubts about domestic commitment to the programs, there was a clear need for closer watching for the risks**. The second PRGF-supported program, adopted in May 2001, did not fully meet the required standards, but the authorities were given the benefit of the doubt at the outset of the PRSP/HIPC era in view of the authorities' noteworthy efforts to put together their PRSP and implement the strategy, as well as pressures to bring a number of countries to the decision point. In the event, the program went off track soon after its approval in May 2001, precluding the timely completion of a review based on the end-

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[12] It is difficult to distinguish quantitatively between the impact of exogenous shocks and failures in implementing critical policy measures to explain the slippages. Nonetheless, the delays in tackling the deep-rooted problems in the water and electricity sectors have subdued growth in these sectors and industrial activities, shaving an estimated 1 percentage point annually in 2000–03 from projected overall GDP growth. The absence of support in the marketing of fish products and the lack of progress in trade facilitation also lowered growth. The shortfall in exports during 1997–2003 has been almost 18 percent of projections or US$147 million on an annual average basis, mostly due to lower-than-anticipated prices of mining products, but also due to lack of new investments in the mining sector because of an investment-hostile environment.

September 2001 test date. Only following the implementation of a four-month consolidation plan was the review concluded in July 2002. At that time, there were already signs of impending further slippages. In retrospect, the risks raised during this review did in fact come about, and no review was completed since July 2002.

Program design

35. **At the level of program design, some objectives appear to have been overambitious.** Export projections were too optimistic. While the decline in some prices in the mining sector could not have been foreseen, delays in undertaking planned investments, notably in the mining sector, have also played a role. Such shortfalls had an impact on the continued nonobservance of the NFA target and, to some extent, the shortfall in fiscal revenue. Similarly, overoptimistic assumptions for the disbursement of external assistance under the programs may have led to the setting of unrealistic targets; since these shortfalls mostly reflect failure to observe donors' conditions, at least part of this problem concerns program compliance.

36. **Contingency plans to deal with shocks were inadequate**. The programs had built-in adjustment mechanisms to address shortfalls in external assistance. However, they had no contingency plans to deal with shortfalls in domestic revenue or in foreign exchange reserves resulting from adverse exogenous shocks or spending pressures emanating from genuine security threats. The existence of such plans could have encouraged the authorities to seek long-term instead of ad hoc measures to meet the program targets at a given test date—the use of ad hoc measures weakened program implementation downstream, resulting in delayed reviews.

37. **On the structural side, some of the benchmarks were very limited compared with what the reforms were supposed to achieve**. In particular, in the judiciary area, in 1997 the Bank had a judicial capacity building program that included the reforms mentioned in Table 2. The Bank dropped this program because of lack of commitment to reforms from government officials. As a result, the implementation of the action plans was not monitored because there was no follow-up conditionality by the Bank. The Fund's programs continued to stress the need for judicial reforms, but did not take them up in their conditionality to abide by the division of labor between the two institutions.

38. The discussion above suggests that, while adverse exogenous shocks and weaknesses in program design explain in part the observed poor performance, institutions in general and the political system in particular have played an important role in policy choices and the consequent outcome. Even though there is an understanding that better policies and reforms would help the country meet its broader social goals, in hindsight often the authorities did not

share the same objectives. The political system, in place, and the political leadership's discretion have enabled policy choices with socially suboptimal outcomes.[13]

III. Lessons and Policy Challenges For the Medium Term

39. **The main lesson of the experience under IMF-supported programs in Guinea is the need for ensuring ownership and commitment at the highest level of government at the onset of the program**. Without such commitment, experience is that program implementation will remain haphazard and policies will be halted or reversed at the earliest sign of political costs. In this regard, the Fund should allow sufficient time for evidence for strong commitment to be shown, even if this means interrupting programs for an extended period. On a positive note, the UN-sponsored initiative to advance stability in the region adopted in 2003 should help relieve the economic toll and the need for political expediency in defense matters.

40. **Strong ownership and commitment will need to be demonstrated by early and decisive progress in implementing structural reforms in key areas as corruption, the utility sector and the judiciary and legal system.[14]** Without such progress, private investment and the necessary diversification of production and exports will not be achieved and exports, investment, revenue and the economy as a whole will remain highly vulnerable to external shocks. Under these circumstances, clear evidence of significantly strong commitment to progress on the structural front should be required before launching a macroeconomic program.

41. **Closely related to ownership is the need to pay more attention to poor governance in future programs.** Corruption remains a major impediment to improving the fiscal situation, and will, if not addressed forcefully, continue to undermine any reform efforts in revenue and expenditure management. To this extent, future Fund-supported programs should emphasize specific actions to reduce corruption in the customs and tax revenue offices, with transparent and monitorable actions. In particular, the adoption of WAEMU's CET in 2005 will eliminate all the ad hoc taxations of imports accumulated over the years, which are the main sources of corruption at customs. Also the May 2004 FAD tax

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[13] The poor policies of the past two years, which have led to the suspension of budgetary assistance from many donors have been very onerous to the population. In particular, owing to the discretion of the political leadership and the lack of independence of the central bank, the government has continued its expansionary policies financed by monetary emission. This has fueled inflation, which has further hurt the poor.

[14] The World Bank has indicated that, should the authorities demonstrate political will to fight corruption, it may, through its Capacity Building for Service Delivery (CBSD) program, support reforms to improve the judicial system.

administration technical assistance mission identified specific areas to focus on in future programs to reduce corruption.

42. **A key lesson is the need to incorporate ex ante contingency plans in future programs as a precautionary cushion should new risks materialize.** This would help the Fund to better assist the authorities in maintaining the adjustment efforts in the face of exogenous shocks, or in case key assumptions turned out to be overly optimistic. This, in turn, will require greater effort at prioritizing expenditures and at integrating the macroeconomic framework into the rest of the poverty reduction strategy, as laid out in the PRSP. Experience to date suggests that more work is required to complete the costing of the various antipoverty programs and to integrate them fully into the budget in order to strengthen budget monitoring and evaluation procedures. Moreover, future programs should seek to adopt more realistic assumptions on key macroeconomic variables, such as GDP growth, exports, and external financing.

43. **Based on a broadly supported domestic long-term development strategy, the main economic challenges for Guinea are to diversify its economy and to mobilize sufficient resources to meet the Millennium Development Goals**. Most of the necessary policies have already been identified in earlier programs and the PRSP. In this context, it would be important for the authorities to implement policies to allow for the resumption of PRGF-supported programs. This would, conditional upon satisfactory performance, pave the way for attainment of the completion point under the HIPC Initiative, and increased availability of resources for poverty reduction.

44. **A further challenge for the authorities is to ensure that decentralization is implemented efficiently.** Fiscal decentralization is an integral part of the government's poverty reduction strategy as a key measure to bring the government closer to the people. However, it requires strong institutional capacity at the local level, careful planning over time, and effective monitoring to curb corruption, waste, and misappropriation of resources transferred to local governments.

IV. FUTURE FUND RELATIONS WITH GUINEA

45. **Guinea continues to have considerable macroeconomic imbalances and structural problems in the core areas of the Fund's expertise, warranting continued close involvement**. In addition, Guinea's external debt continues to be unsustainable, requiring a solution in the context of the HIPC Initiative, and thus a PRGF-supported program. Key elements of the remaining reform agenda fall within the Fund's core areas of expertise and responsibility, and Guinea could greatly benefit from the Fund's technical assistance to strengthen capacity.

46. **Despite the need for Fund assistance, a new financial program should be made contingent upon clear evidence and track record of commitment to its objectives at the highest levels of government.** To this extent, discussions on a new PRGF-arrangement

should be preceded by an extended staff-monitored program (SMP). The SMP should aim at addressing the present macroeconomic imbalances, and emphasize governance and transparency in the fiscal sector. In addition, in close cooperation with the World Bank, the authorities should show strong progress in advancing the structural reform agenda, including in areas with direct impact on the financial situation, such as the utility sector.

47. **Guinea's limited progress toward macroeconomic stability, and the scale and duration of the reforms to be addressed, suggest that the country is not expected to graduate soon from the use of Fund resources.**

Table 1. History of IMF Lending Arrangements

(In millions of SDRs, unless otherwise indicated)

Type	Approval date	Expiration date	Amount Approved	Amount Drawn
PRGF	May 02, 2001	May 01, 2004	64.26	25.70
ESAF/ PRGF	Jan 13, 1997	Jan 12, 2001	70.80	62.94
ESAF	Nov 06, 1991	Dec 19, 1996	57.90	46.32
SAF	July 29, 1987	July 28, 1990	40.53	28.95
Standby	July 29, 1987	Aug. 28, 1988	11.60	0.00
Standby	Feb. 03, 1986	Apr. 02, 1987	27.00	21.00

Source: IMF, Finance Department.

Table 2. Guinea: Structural Reforms Scheduled in Selected Key Sectors During 1997–2003: Unfinished Agend

Sector	Envisaged Actions	Schedule timing of implementation	Status/Progress
Fishing	(i) Strengthening fisheries research activities and the management of fishery resources;	1997; 1998–2000	No progress.
	(ii) support the marketing of fish products through the construction of storage, processing, and packing facilities;	1997; 1998–2000	No progress.
Mining	Create an environment conducive to private sector development by revisiting existing regulations, reducing government's ownership, and promoting private investment.	1997–2000	Very little progress. Expected foreign direct investment in the mining sector has yet to materialize, mostly because of institutional problems.
	Adopt an action plan to improve the working conditions of members of the judiciary.	1999–2001	Not implemented. Attempts to improve working conditions of magistrates initiated in 2003.
Judicial reforms	Adopt an action plan to strengthen the functioning of institutional mechanisms established to enforce the rules of conduct to be followed by members of the judiciary.	1999	Unclear whether plan was adopted. No improvement in the administration of justice.
	Accelerate loan recovery procedures and improve arrangements for providing loan collateral.	1997–99; 1998–2000	Not implemented. Difficulties in the area continue to hamper the financial sector.
Trade	Harmonize the custom tariff with those of other countries in the sub region.	2000; 2000–01	Not implemented. Adoption of the WAEMU CET now scheduled for 2005.
Fight against corruption	(i) elaborate a strategy to fight corruption.	1999–2000	Anticorruption Committee created in 2000. Almost no progress in the fight against corruption.
	(ii) put in place an action plan.	2000–01	Vested interests have stalled prosecution of identified cases of corruption.
Energy	(i) increase private sector participation in energy production in the Conakry region.	1997–98; 1999–2001	No progress. Unreliable electricity supply continues to hamper private sector activity.
	(ii) implement electrification program for interior cities.	1998	Very little progress.

Source: IMF, African Department.

Table 3. Guinea: Selected Economic and Financial Indicators, 1996-2004

	1996	1997		1998		1999		2000		2001		2002		2003		2004	
		Prog. 1/	Real.	Prog. 1/	Real.	Prog. 1/	Real.	Prog. 1/	Real.	Prog. 1/	Real.	Prog. 1/	Real.	Prog. 1/	Est.	Prog. 1/	Proj.
								(Annual percentage change; unless otherwise indicated)									
Income																	
GDP at constant prices	5.1	4.8	5.0	5.0	4.8	3.7	4.6	5.0	1.9	3.3	4.0	5.4	4.2	5.7	1.2	6.5	2.6
GDP at current prices	6.1	9.5	6.7	9.8	7.1	7.8	8.2	9.3	13.2	10.9	8.9	10.7	7.1	11.1	13.7	11.2	19.2
GDP deflator	0.9	4.5	1.7	4.4	2.2	3.9	3.4	4.1	11.1	7.4	4.7	5.3	2.8	5.4	12.3	4.7	16.2
Consumer prices																	
Average	3.0	5.0	1.9	4.0	5.1	4.5	4.6	5.8	6.8	9.6	5.4	4.2	3.0	3.0	12.9	2.8	16.6
End of period	2.1	5.0	5.3	3.5	4.5	5.4	6.2	4.0	7.2	9.4	1.1	3.2	6.1	3.8	14.8	2.0	18.0
External sector																	
Exports, f.o.b. (in U.S. dollar terms)	-6.7	14.0	1.8	9.5	3.7	6.4	-2.7	9.1	4.9	11.5	8.4	10.6	-2.0	8.1	2.3	9.3	1.2
Imports, f.o.b. (in U.S. dollar terms)	0.1	11.7	-6.9	7.7	7.4	1.5	-4.1	9.3	4.3	16.7	-3.7	6.6	6.1	6.7	-3.0	8.1	0.0
Terms of trade																	
Percentage change	-0.3	0.4	15.4	1.1	8.0	-6.7	-8.5	-0.9	-7.9	-3.8	7.7	7.6	2.3	5.5	-2.9	3.6	-4.0
Average effective exchange rates (depreciation -)																	
Nominal index	2.0	...	0.0	...	-7.4	...	-9.0	...	-13.8	...	-5.8	...	-3.3	...	-11.3	...	...
Real index	2.3	...	-0.1	...	-4.1	...	-6.0	...	-10.1	...	-3.0	...	-2.3	...	-2.7	...	...
Money and credit																	
Net foreign assets 2/	-7.0	22.9	20.4	11.6	5.6	-4.5	-6.9	14.8	-4.8	25.4	12.6	...	-11.9	...	-9.4	...	-4.6
Net domestic assets 2/	10.1	-10.4	-3.1	-2.6	0.5	14.1	10.1	-4.8	28.2	-16.9	2.1	...	31.2	...	44.7	...	24.6
Public sector (net) 2/	10.6	-11.5	-4.3	-8.3	-3.4	10.0	10.8	-5.1	21.5	-13.0	3.7	...	34.2	...	34.0	...	19.1
Private sector 2/	2.2	9.0	-0.2	10.1	7.9	7.0	8.6	4.8	5.0	4.0	4.3	...	3.5	...	8.6	...	2.9
Broad money	3.1	12.5	17.3	9.0	6.1	9.5	8.8	10.0	23.4	8.5	14.8	...	19.2	...	35.3	...	20.0
Reserve money	-2.2	9.8	15.1	11.3	14.0	10.7	15.0	8.7	17.0	5.3	11.0	...	18.3	...	27.4	...	13.7
Velocity (GDP/average year-end M2)	11.3	11.8	10.9	10.8	10.5	10.6	10.6	10.5	10.3	9.3	9.4	...	8.6	...	7.7	...	7.2
Central government finances																	
Total revenue and grants	13.4	15.2	14.6	14.5	14.1	12.3	13.1	13.6	13.2	18.7	14.7	19.4	13.8	20.0	13.2	20.4	12.4
Of which: nonmining revenue	7.5	8.9	8.5	8.7	8.3	8.1	8.3	9.2	8.2	10.1	8.5	10.6	9.8	11.4	9.0	11.9	9.1
Current expenditure	9.0	9.0	9.1	8.4	8.7	8.5	8.9	9.0	9.3	12.1	11.6	11.2	12.2	11.4	12.9	12.1	9.8
Capital expenditure and net lending 3/	7.4	8.7	8.4	9.0	6.0	6.8	7.2	7.8	7.2	9.8	7.2	9.5	6.0	9.4	5.5	9.6	5.2
Overall budget balance																	
Including grants (commitment)	-3.0	-2.5	-3.0	-2.9	-0.7	-3.0	-3.0	-3.2	-3.2	-3.2	-4.1	-1.3	-4.4	-0.8	-5.1	-1.3	-2.6
Excluding grants (commitment)	-6.2	-5.7	-6.0	-5.9	-3.6	-4.8	-5.3	-5.3	-5.5	-8.6	-7.5	-6.8	-6.2	-6.3	-7.9	-6.4	-4.1
Primary balance	1.3	3.1	2.9	2.9	2.6	2.4	2.4	2.7	2.5	0.8	0.6	1.3	0.0	1.6	-1.6	1.2	1.6
Gross investment	23.1	14.2	23.6	22.3	21.0	18.2	22.1	19.2	19.7	24.2	15.3	23.9	13.1	24.0	9.9	24.1	10.5
Government 4/	7.4	6.5	8.2	6.5	5.6	5.0	7.2	5.5	4.9	9.4	4.9	9.1	4.0	9.2	3.8	9.4	3.6
Nongovernment	15.7	7.7	15.4	15.8	15.3	13.3	14.9	13.7	14.8	14.8	10.4	14.8	9.1	14.7	6.2	14.7	6.9
External current account balance																	
Including official transfers	-8.5	-4.8	-7.0	-4.7	-8.5	-3.3	-7.6	-3.6	-6.4	-2.6	-2.7	-2.6	-4.3	-1.9	-3.3	-1.3	-2.9
Excluding official transfers	-8.9	-8.0	-7.2	-7.7	-10.2	-5.9	-8.3	-6.3	-7.2	-6.7	-4.8	-6.1	-5.6	-4.9	-4.0	-4.2	-3.7
								(In percent of export earnings)									
External public debt	423.3	398.0	422.9	297.6	450.6	349.4	465.0	335.2	443.9	376.9	396.7	344.7	387.9	321.5	420.9	294.9	399.3
								(In millions of US dollars; unless otherwise indicated)									
Exports 5/	618.5	793.0	629.5	843.0	653.0	754.5	635.7	823.4	666.6	774.5	722.8	856.2	708.5	925.7	724.5	1,011.7	733.0
Imports 5/	583.7	796.9	543.2	821.0	583.3	580.1	559.4	634.3	583.3	648.1	561.9	690.6	596.2	736.8	578.1	796.2	578.1
Overall balance of payments	-133.3	-34.0	74.1	-74.9	64.4	-118.6	-33.0	-85.9	68.5	-80.4	-25.1	-79.4	-83.7	-44.2	-93.7	-10.4	-62.4
Net foreign assets (central bank)	71.6	115.0	118.1	143.2	112.4	84.2	71.8	109.7	28.5	98.4	60.7	…	26.4	…	-10.2	…	-28.3
Gross official reserves (in months of imports)	2.6	2.9	2.6	3.4	3.1	2.9	2.8	3.2	2.0	2.6	2.7	2.6	2.3	2.7	1.5	2.8	1.2
Nominal GDP	3,884.5	4,325.9	4,144.4	4,707.0	4,438.2	5,043.0	4,802.2	5,512.0	5,436.9	5,915.4	5,919.7	6,564.4	6,340.3	7,313.5	7,209.8	8,151.1	8,595.0

Sources: Guinean authorities; and staff estimates and projections.

1/ For the period 1997-2000 program figures refer to those of the different annual arrangements, while for 2001-04 program figures refer to the targets of the original 3-year program under the arrangement approved by the Executive Board in May 2004. Some of these original program targets may have been revised in light of observed or anticipated developments.
2/ In percent of broad money stock at beginning of period.
3/ Includes expenditure for restructuring.
4/ Fixed capital formation.
5/ Merchandise trade figures only.