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INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

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Washington, D.C.

The meeting of the Executive Directors was convened at 10:02 a.m. in the Board Room, 1818 H Street, N.W., Washington, D.C., Mr. Barber B. Conable, Chairman, presiding.

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C O N T E N T S

[redacted]

MR. CONABLE: [redacted]

Let's move on now to Rwanda. Item two is a proposed first structural adjustment credit in the amount of 67.5 million SDR, or $90 million U.S. equivalent, to Rwanda.

Mr. Abu-zobaa, a Division Chief of the African Department of the IMF, is attending this meeting. We welcome him.

Mr. Devaux is a Country Officer in the Africa Region, and he is going to introduce the proposal for us on this Rwandan loan.

Mr. Devaux.

MR. DEVAUX: Mr. Chairman, Members of the Board: The credit before you is the first structural adjustment operation in Rwanda. It took several years of intensive

dialogue for the government to request the help of the Bank and the IMF in preparing an adjustment program and to agree on a viable policy framework which provides the basis for this credit. The policy framework paper was discussed by the Committee of the Whole on April 23.

As we reported then, a draft policy framework paper had just been negotiated when in October 1990 the country was invaded by Tutsi refugees from Uganda.

Diplomatic efforts with neighboring countries to find a political solution to the conflict and President Habyarimana's decision to initiate a process of national reconciliation and political reform led to a formal cease fire, which was signed on March 29.

The cease fire has been generally respected, despite skirmishes along the northern border. Since that date, the political situation has improved but still remains fragile. The political reform process is progressing well: a new constitution which opens the way for multi-party elections was signed into law on June 10; several new parties have made known their intention to be registered as soon as the law on party politics is adopted; a series of amnesty measures have been undertaken, including the release of about 8,000 political prisoners.

Multi-party elections are expected to take place before the end of the year. Some progress has also been registered on finding a political solution to the refugee issue. The meeting requested by the Heads of State in Dar es Salaam took place in May in Geneva and it was agreed to proceed with a census of all refugees as a first step to the preparation of an action plan.

On the economic front, Rwanda had been a good performer in the 1970s when growth averaged 4 percent per year. However, in the 1980s the authorities pursued inappropriate policies to deal with external shocks, especially the decline in the price of coffee, the main foreign exchange earner.

By 1990, the incentive structure had become highly distorted with widespread price and foreign exchange controls. The exchange rate became highly overvalued. These policies led to losses in competitiveness, the development of inefficient economic activities and a decade of steadily declining per capita income.

The government took a long time to arrive at the conclusion that an adjustment program was necessary to establish the conditions for a resumption of economic growth. This long internal debate has allowed an internalization of

both the nature and the pace of the reforms. The proposed credit will support the government's structural adjustment program described in the PFP.

The main objectives of the program are to stabilize the economy, create an enabling environment to improve Rwanda's competitiveness, promote a better allocation of resources, lay the foundation for an export led growth, and enhance living conditions for the Rwandese people.

Specifically, this credit will support measures: establish and maintain a competitive exchange rate; introduce a more liberal foreign exchange allocation and trade regime; rationalize import tariffs; liberalize domestic trade; simplify and streamline the regulatory environment; alleviate institutional and production constraints in the coffee and energy sectors; improve public resource management, including the introduction of a rational process of public expenditure programming; and initiate policy reforms dealing with labor legislation and civil service.

Finally, as in the case of the Comoros adjustment, which was approved by the EDs last week, the Rwanda SAL incorporates in its design a satisfactory social safety net compatible with a sound macroeconomic framework.

The government has demonstrated its firm commitment

to the reform program supported by this credit by taking several politically sensitive measures upfront. Some of the important actions already taken include a devaluation of 40 percent in foreign currency terms, a 79 percent increase in the price of petroleum products, the introduction of a liberalized import regime for a majority of imports, the abolition of import prohibitions, the elimination of most controls on profit margins and fixed price, and a liberalization of interest rates.

The proposed credit is expected to contribute to the restoration of internal and external financial and economic equilibria, and the proposed measures to improve the incentive system should stimulate private sector activity which is necessary to restore economic growth and employment creation.

The proposed credit is the centerpiece of the Bank's country assistance strategy discussed by the Executive Directors last December. It will be followed by two other adjustment operations: a financial sector adjustment credit and an agricultural sector adjustment credit aimed at deepening sector reforms to stimulate a supply response.

The program supported by the proposed credit was developed in close collaboration with the IMF, the ADB,

Belgium, Switzerland and several other bilateral partners who have affirmed their support to Rwanda in the framework of the Special Program of Assistance for Africa.

During a special donors' meeting in March, donors provided firm indications of commitments to fill the financing gap for 1991.

Thank you, Mr. Chairman.

MR. CONABLE: Thank you very much, Mr. Devaux.

Now, what questions do we have on this proposal?

Mr. Cox.

MR. COX: Thank you, Mr. Chairman.

It wasn't my intention to go first, but I guess here I am.

MR. CONABLE: Be brave.

MR. COX: I usually am.

MR. CONABLE: Pioneering carries a great premium.

MR. COX: That's what happens when you grow up in Wyoming, Mr. Chairman. You become a perpetual pioneer.

MR. CONABLE: Yes.

MR. COX: Thank you.

The economic program outlined here seems generally on target. We note that the problem of overvalued exchange rates is a factor in several contexts, specifically the need

to improve export competitiveness and to reduce the current account deficit.

It is, therefore, of critical importance that the Rwanda franc be maintained at an appropriate level and that a non-discriminatory foreign exchange allocation system be established, as required for the second tranche release of this loan.

It is critical to get control of the fiscal deficit and thereby of domestic indebtedness, especially bank borrowing.

The program establishes a detailed agenda for reducing the deficit, but does not again mention the subject of domestic debt after referring to the program on page 4. Does the staff believe that this is an issue requiring further attention? If so, perhaps additional comments could be made there.

Given the need to improve export competitiveness, we wonder why export taxes are to be retained on coffee. This is referred to on page 6, paragraph 17.

We applaud the emphasis given to encouragement of the private sector and to price reforms as a partial means to that end. In addition, we applaud the detailed timetable on page 40 for the public enterprise project. Given the severity

of Rwanda's fiscal problems, however, the schedule for diagnostic studies on page 41 strikes us as quite relaxed. Shouldn't and couldn't this be accelerated?

Because the reform on import policy and foreign exchange allocation is an interim measure for moving to the open general licensing system, there is a need for institutional strengthening to ensure that the liberalization process moves forward in a sustained manner.

As there are many reform areas involved, we are concerned about the government's institutional capacity to implement the reforms in a timely manner to monitor and assess their effects and to make necessary modifications.

We would encourage the government to seek needed technical assistance in the short run, while attempting to build up its own national capacity over time.

Thank you, Mr. Chairman.

MR. CONABLE: Thank you, Mr. Cox.

Mr. Patai.

MR. PATAI: Thank you, Mr. Chairman.

We fully support the credit before us. The present structural adjustment program is very timely and addresses the problems of the country comprehensively.

Let me point out three major elements. Adjustment

of the exchange rate to the external situation, long advocated by this Chair, is and will continue to be a major element of this program.

Likewise, the elimination of import restrictions and establishment of an open general licensing system represents important changes which donors are eager to support.

The introduction of a rolling public investment program will provide a useful framework for coordinating multilateral and bilateral aid and increasing its efficiency and benefit to the country.

Two questions: In light of the risk presented by Rwanda's weak institutional capacity for implementation, I would like the staffs to elaborate on the measures taken to address this problem. In the same vein, what measures have been taken to improve the relatively low level of disbursements in the Bank's project lending?

Second, would not establishing a minimum level of 10 percent for all imports tariffs involve an increase in the tariffs on capital goods which could be harmful to the development of a diversified private sector?

Thank you.

MR. CONABLE: Thank you, Mr. Patai.

Mr. Baijal.

MR. BAIJAL: Thank you, Mr. Chairman.

I am fully supportive of this operation. There is, however, one question which is on the basis of reading of Table 1 and Table 3. Maybe it is answered properly but, if it is a dumb question in terms of what Mr. Potter said, it is because I have not been able to read the whole thing very carefully.

Now, the question was that if you look at -- I couldn't find the terms of trade calculation anywhere, how they have moved. But if one looks at the export volume growth between 1986 and 1990 or so, the export volume has increased by about 36 percent.

But the export receipts have gone down even in nominal terms. It is a very disastrous situation.

Imports have gone down by 16 percent, but the import payments have more or less remained at the same level as in 1987.

Now, under this situation if we are going to have -- obviously, these exports are impoverishing the country almost continuously. And we are going to encourage an export system more by making adjustment in the exchange rates and so on. Now, if it is not accompanied by a very, very strong

program of diversification or improvement in productivity or something like that, I think this is going to make a very poor country still more poor.

So, all that we are told here is that the diversification program should be done, and there is a timetable which says that by 1991 it will be done. What is the content of the diversification, what is the role which the Bank is playing in giving them due assistance for diversifying their economy so that they don't really keep on exporting whatever little net wealth they have?

Thank you, Mr. Chairman.

MR. CONABLE: Thank you, Mr. Baijal.

Mr. Al-Assaf.

MR. AL-ASSAF: Mr. Chairman, I also support this operation. I think it addresses the main issues facing the country.

I have a couple of comments, one on the health sector. This has been subject to discussion bilaterally with the staff, but I think this is an important area that the authorities should look into, especially, as the report indicates, that the country is facing diseases as AIDS and malaria, and some efforts should be given to this sector.

The other is on energy. I welcome the intention to

exploit the methane gas in Kivu Lake. And I think that will help the country first from an environmental point of view and, second, from foreign exchange.

But I don't understand the other aspects of the energy where the country attempts to make exports more competitive, as Mr. Cox mentioned, and diversify the economy while at the same time increasing the costs of other sources of energy. I think this is again a point I mentioned before.

Thank you.

MR. CONABLE: Thank you.

Monsieur de Fontaine Vive.

MR. DE FONTAINE VIVE: (Interpreted from French.) Thank you, Mr. Chairman.

I would like to say immediately that we support obviously without any reservation the document before us today. And I would like today to limit my comments to the content of the program, going rather quickly on the macroeconomic framework since less than two months ago we had an opportunity to discuss the PFP during our meeting of April 23 last.

So, regarding the macroeconomic framework, I will make only three observations on three traditional subjects: first, the importance in controlling budgetary expenditures

in this country, which is heavily dependent on external aid; regarding currency to recall our concern of having not only a decrease in the growth of the aggregate but also to have positive interest rates, but this obviously will be part of the structural adjustment loan in financial sector; and finally, regarding the exchange rate, in view of the important devaluation.

A question is raised about the possibility of a consolidation phase since the tables referred to by Mr. Baijal do show that we can have a phase of stabilization of the exchange rate between the Rwandese franc and the dollar. This is compatible with the program before us today.

Therefore, I would like to concentrate my intervention on the elements which are relating to the content, first, to welcome the importance granted to the social and population component of the project itself, the project which is next on the agenda under the Special Procedure, which fits perfectly this logic. We consider as particularly welcome the safety net which will be put in place under this problem.

The second source of satisfaction is also the emphasis placed in a rather diffused way on the technical assistance to help with the problem of institutional capacity which is chronically weak in this country. Perhaps this

diffused character could disappear if we had a more voluntary presentation of the technical assistance given by the World Bank Group to Rwanda.

The third element of satisfaction, halfway between the two points, which is the emphasis placed on the greater flexibility of inputs, particularly the mobility of labor which is one of the components of this program.

The fourth element on which I would like to come back, a question for the staff under the chapter "Reform of the Public Sector" on page 17, it is indicated there that the public enterprises will be part of the privatization program, but nothing is said about what will happen on the exoneration of taxes for this public enterprises.

Is this already done or is this part of this program? Paragraph 55 says nothing on this point, while paragraph 54 talks at length on the disappearance of all the public enterprises, including whether or not they are profitable in the country.

Another comment which I note in paragraph 71, page 22 of the document, which traditionally in all adjustment programs indicates the risks of a project and, therefore, I am rather surprised, in fact, in finding in paragraph 71 which implicitly involves the will of the authorities of

Rwanda to develop this adjustment program, while saying quite the contrary, and it seems to me, for example, in the project we have just examined regarding Hungary -- I will refer to it quickly -- we haven't felt the need of having questions on the will of the authorities in the country to implement the program.

I thought I understood that, if the management was giving us a product, it was convinced of the will of the authorities to implement this program. Therefore, I would like to know why we find this in paragraph 71.

Finally, to indicate to you that we expect with interest and some impatience the next two structural adjustment operations. To the extent that the reform in the financial sector and agriculture appear to us quite indispensable, to ensure a durable growth base for Rwanda in the administration last April and in the IMF concerns some questions which were expressed as to the realism of the growth rate which is indicated in the PFP, which is the basis of this structural adjustment program.

Thank you, sir.

MR. CONABLE: Thank you, Monsieur de Fontaine Vive.

Mr. Rehm.

MR. REHM: Thank you, Mr. Chairman.

I support the first structural adjustment program for Rwanda. It is ambitious and I can only hope that the envisaged growth rates of GDP and exports will be realized. But there is no alternative to structural adjustment.

Given the difficult situation in the country and the recent ethnic strife, a careful design of the adjustment credit is very important. The emphasis put on measures to alleviate the negative impact of adjustment on the poorest strata of the society is, therefore, very well taken. This will help to make more sustainable the structural adjustment process that Rwanda is embarking upon.

Allow me one observation that I have made before, and that is of some important to Rwanda but also to other countries in the regions. The measures envisaged in the SAL to promote the private sector are necessary indeed. But this might not be enough.

Right now, Rwanda and the neighboring countries are producing more or less the same products. So, the potential of trade in the area is probably rather small.

But with diversification in the long-run there will be a need to export to neighboring countries and, therefore, there might be a case for the Central African Economic Community. Without open borders to neighboring countries,

the potential to create enough jobs for the fast-growing population might be rather limited.

Maybe such a concept could be realized in the framework of the Communite Economique des Pays des Grands Lacs. The countries of the region need encouragement to think about such a concept.

I want to close with a remark regarding the first population project that is on our agenda under Special Procedure. Reading this document really made clear to me how important a successful population policy is for Rwanda. Without putting a cap on population growth, all the adjustment efforts will lead to nothing in the long-run.

I strongly support the population project.

Thank you, Mr. Chairman.

MR. CONABLE: Thank you, Mr. Rehm.

I think there will be further comment on that last loan, the population loan.

We have a number of issues here before us, Mr. Devaux, starting even with the coffee export tax. Will you address these problems?

MR. DEVAUX: Concerning the domestic tax, obviously it is a mounting problem in Rwanda, but we understand that a number of donors are making special provision as part of the

use of the counterpart funds of their balance of payments assistance to earmark those funds for the reduction of the domestic debt. Therefore, this problem should normally not be eliminated and be reduced.

The export tax on coffee can be criticized in the sense that it may reduce --

MR. CONABLE: It makes coffee less competitive.

MR. DEVAUX: It makes coffee less competitive. On the other hand, it is the only way to tax a large sector of the economy. In fact, there is an income tax which is perceived at the time the product leaves the country. And, therefore, it is very embarrassing to eliminate a tax which is, after all, the normal contribution of a sector. There are other ways to make it more competitive.

Concerning the private sector, the credit recognizes that improving the private sector is very important, but that is certainly not the only thing. We are trying to establish the proper framework for private sector development.

Concerning the public enterprise projects, the current diagnostic studies are difficult to accelerate because we need, first, to establish a strategy and to have the proper legislation. And the government has been extremely timid in the past in moving on the public enterprises.

In fact, some of those studies can be advanced, but a number of them, they have very strong resistance for various reasons. And we don't think we can go faster than has been indicated.

We agree with you on the need for technical assistance to reinforce the institutions, especially in the establishment of the OGL. We did not include it in this credit, number one, because we have already a couple of technical assistance credits which we can use to help the government and, secondly, some of our partners are specifically addressing this issue. Our colleagues from USAID are presenting an adjustment credit to support this one, which has a technical assistance component, to precisely have the government establish and monitor the OGL.

This goes to the question of the next speaker on the weak institution capacity. We are all concerned with the weakness of the institutions, and I think a number of donors are trying to do their best to increase that capacity. In fact, this SAL has been designed in conjunction with a number of partners. Not only the USAID was part of the appraisal mission, but the Belgians, the Canadians, the Swiss and everyone is trying through their own bilateral program to improve the institution and the institutional capacity of the

country.

The level of disbursements in Rwanda has been very low in the past few years. We are very conscious of that and we have undertaken last summer steps to improve the rate of disbursements.

Number one, we had a seminar on disbursement procedures for Bank credit. The administrative procedures as to weakness of institutions in Rwanda are sometimes cumbersome and we had to remind them how they should ask for requests of disbursements of Bank loans.

Secondly, the procurement procedures in Rwanda are extremely delicate and cumbersome, and we also during the same seminar had a special session on procurement procedures on Bank loans.

Normally, we should have seen some impact of those seminars if the war had not prevented the implementation of a number of projects over the last few months.

One speaker mentioned the imposition of a 10 percent minimum tariff on all imports as an obstacle to industrialization and investment. We don't think it is fair to exempt capital goods from any import tax. The 10 percent across the board tariff is essential to manage to reduce the budget deficit.

One speaker mentioned that he could not find any statement on the deterioration of the terms of trade. We are sorry we did not have something on the table, but we can tell you that the terms of trade have been seriously deteriorated over the last five years on account basically of the decline in coffee prices.

In fact, the same speaker was indicating that he was concerned with the decline of exports in value, and the export was increasing in volume, in fact just reflecting the sad situation of coffee prices which have been declining over the last few years.

We obviously are concerned about the program of diversification and these actually create the environment for this diversification. What we see in a country like Rwanda is an industrialization towards exports, an export-led growth. That is what we are looking at.

We would like to take advantage of the differential of wages between Rwanda and some industrialized countries in order to get some kind of industrial development a la Mauritius. Obviously, it takes time. The experience of Mauritius shows us that the first measures were established in the late 1960s and the country could only benefit by the early 1980s.

It takes time to have the right kind of framework, the right kind of incentive to attract foreign investors. The foreign investors are critical in this kind of operation because, number one, they provide certainly capital for investment, but also they provide the know-how which is important and, more important, the marketing system. Without the proper marketing system, there is no way you can export.

So, what we have been doing is to establish the proper framework for Rwanda, to get a lower exchange rate, liberalize the economy, open up the borders, try to establish the right kind of tariffs which are the preconditions for any kind of development.

Now, we know that it will take time for the industrial development to take place. In the short-term we are working on improving coffee production, in improving tea production, in trying to diversify agriculture, and that is one of the objectives of the reform program on coffee that we have in this program, but also of the operations of agricultural structural adjustment which is next in the program.

You mentioned the problem of the health sector. We are very concerned about the health sector and in the social safety net. One of the key things we took care of was to make sure that the level of delivery of the health sector

will remain at least the same as the existing one.

On top of that, we made a special provision to make sure that the resource allocation for the purchase of medicine will be considerably increased.

On energy, we are obviously trying to help the government to develop the gas methane project. We have a sector energy project in our lending program, and this is going to be dealt with in that context.

The tariff increase in electricity is not at all incompatible with the effort to diversify and to industrialize. The problem is that we cannot afford to have the electricity company to lose money. At this juncture, a large share of the electricity use in Rwanda is imported from neighboring countries, and is sold at a price which is below the price of companies. We have to put back a reasonable company on a financial situation which is appropriate.

Concerning the risk, we raised the question of the risk not because we have a doubt that the government will implement the program; otherwise, we will not have presented it to the Board. But there were a number of important considerations in the case of Rwanda.

First of all, Rwanda has been extremely reluctant for a number of reasons for a number of years to embark on an

adjustment program. So, given those hesitations which took four to five years, we felt it was important to reassure the Board that this period of hesitation was actually the reason why we believe the government is committed to the program.

On top of that, the government demonstrated its commitment by taking some very, very politically sensitive measures in the midst of the difficult political situation. We have absolutely no doubt this program will be implemented.

Interest rates: Yes, of course, we are looking for positive interest rates. At this juncture, interest rates are positive in Rwanda. The inflation, the latest figures of inflation shows us an inflation rate on an annual basis of 15 percent. The interest rates are 19 percent. They are positive for the first time.

Now, obviously, we will have to review it and the financial sector adjustment credit will obviously take care of that.

Exoneration of tax on public enterprises: We don't see any reasons why public enterprises should be exonerated. They are enterprises like any enterprise. There is a need in Rwanda to improve the fiscal situation. All enterprises have to be taxed, either if they are private or public. There is no discrimination. If they have not been taxed in the past,

well it is something which is being corrected.

MR. CONABLE: Mr. Carneiro has something he wants to follow-up on.

MR. CARNEIRO: A short follow-up. I must have heard incorrectly the staff explanation on the coffee export tax. I believe I have heard that the export tax was acceptable as it was the only income tax that was applied to the coffee sector. Can you please clarify this subject, because if this is the case, we are very much distorting some of our basic principles?

MR. CONABLE: What about real estate taxes?

MR. JAYCOX: This country doesn't have real estate taxes except in the cities. This country doesn't have income taxes on small peasants.

The only way that this sector can be taxed is through an export tax on the product. It is easy administratively and it is the only sector in this country. It also is, as a result of devaluation, very profitable, even at the low prices.

In fact, we don't want to not tax this product because we want to diversify. We certainly don't want to have this be a sinecure where everybody can make all the money they need, and they don't have to diversify. So, this is an

economic policy where you tax every productive sector in as uniform as possible way, but with certain incentives built in to diversify, not to privilege this sector so much.

It is the only source of income for the country. It has to be taxed one way or the other.

MR. CONABLE: Wouldn't you also have a goal at diversifying your revenue sources?

MR. JAYCOX: Sure.

MR. CONABLE: Yes.

MR. JAYCOX: But you can do that only if your revenue take is larger than the administrative costs of getting the take. And these things are under very careful review with the IMF and the World Bank staff, looking at these issues of how to raise revenues in a country like Rwanda without dampening economic activity.

There is nothing very secret about it. After the devaluation, I think we should look at what percentage of the world market price is actually going to end up in the hands of the peasants. That is the bottom line because if it isn't adequate, they will not produce coffee.

MR. CONABLE: Mr. Al-Assaf wants to follow up perhaps on the issue of gas or perhaps on the issue of the health sector.

MR. AL-ASSAF: Well, the first one, Mr. Chairman.

I thank Mr. Devaux for the response on the energy. Actually, the electricity rates are important as far as the competitiveness is concerned, but also the other side, the petroleum which, as the document indicates, is substantially higher than national prices, and the rates are already increased by, I think, 67 percent and now the tariff.

The question is obviously there is a budgetary impact -- I see Mr. Abu-zobaa there from the Fund -- this is a very important element. But at the same time, how is this reconciled with the attempts to promote exports? When you increase the inputs, obviously it affects the competitiveness. And how would this increase affect the promotion of exports and the diversification of such exports?

So, there are two sides to that issue: one, the budgetary, which is important; the other is the structural element and especially as far as exports are concerned.

Thank you.

MR. CONABLE: Thank you.

Before we answer that question, we have a follow-up from Monsieur de Fontaine Vive.

MR. DE FONTAINE VIVE: Thank you, Mr. Chairman.

Two short follow-up points. The first one about the

taxation on public enterprises, I never advocated for any exemption. I think my question was misunderstood.

My question was I read in the last sentence in paragraph 54 that all PEs are exempt from income taxes. So, that is your statement about the present situation, and that is what I am challenging. And then when we are turning to the action plan, which is supposed to be described on the following paragraph, which is 55, I don't find anything about that.

That was my question. Why don't we have something about that? Is it an implicit part of the action? That was my question.

My second follow-up is about the risk, the so-called risk about the commitment of the government. The explanation about the slow and the long discussion between the government and the World Bank, among some other donors, is given in paragraph 72 as the third risk. So, I don't see any reason to have this risk about the commitment of the government. As a matter of fact, I was wondering generally if we could avoid such a paragraph in any loans because, as you said, when you are presenting such a loan to the Board, we think you have solved the problem.

MR. CONABLE: Mr. Jaycox, do you want to respond?

MR. JAYCOX: I will just speak to this last point. What was meant to be said on risk was the internalization process, not the will of government, but the fact that the population has been fully brought onboard with respect both to the aims and the trials and tribulations that the population is going to have to go through.

We do not feel that this is done very well in most of Africa. We raised the issue that if the population is not brought onboard in these projects, in these programs, they are not explained to them properly, that, in fact, there will be hitches in the implementation. And this is raised not as a question of political will but a question of internalization.

I think the paragraph has been misinterpreted. This is the paragraph that we were both referring to earlier, I believe. Is it not? Have I responded to the question?

MR. DE FONTAINE VIVE: As usual, we fully agree with Mr. Jaycox about Africa. So, I have no problem, but what he is explaining about internalization, which is quite right, is what you call the third risk on paragraph 72.

MR. JAYCOX: Yes. That is what I thought.

MR. DE FONTAINE VIVE: And I am not changing all this which is really part of the process, because you need

this to be internalized in the process to have the full support of not only the authorities, the government but all people responsible on development of this country.

What I was challenging is the previous one, which is the 71 and which is only about government's willingness. And this one I think could be avoided.

MR. CONABLE: Mr. Aguirre-Sacasa wants to respond also.

MR. AGUIRRE-SACASA: Let me just say two or three things. Number one, the government demonstrated at a very delicate moment, in fact during the moment of greatest fighting back in October, that it was committed to the adjustment program by taking many of the actions that Mr. Devaux referred to.

But there are vested interests in Rwanda, as there are in many countries, that stand to lose from the adjustment process. And some of these groups will clearly continue to put pressure on the government to roll back under the reforms. This happens in every country. And we have seen many examples around the world of countries that embark on an adjustment program and then for diverse reasons, many of them political, fall off of the adjustment track.

Now, we are not meaning to cast any aspersions on

the Government of Rwanda's commitment to reform. In fact, we are very satisfied that the upfront actions that they have taken bode well for the future of the adjustment process there. But there is always a risk -- and that is what we were trying to indicate here -- that at some point a constellation of factors, changes of government, pressures from vested interests in the country could cause the government to pause and perhaps even roll back the reform.

It is very difficult to predict what is going to happen here. We feel comfortable that the Rwandese Government is going to adhere to the reform process, but there is always a small risk, Mr. de Fontaine Vive -- and that is what we are trying to say here -- that government commitment at some future date my slacken.

That's all we are saying.

MR. CONABLE: He is expressing a risk, not a prediction here, I take it.

Monsieur de Fontaine Vive says if there is any danger, why do you --

MR. JAYCOX: Obviously, we think it is a small risk. And, in fact, I think it was put there to show that we believe it is a small risk.

You see, this country has been attacked from

outside by dissidents. They have got their hands full there, both economically and politically. We thought there might be some skepticism on the part of the Board about the political ability of this government to actually carry out this project.

I think we do not feel that way. We feel this government has demonstrated its upfront action, and I think what they were doing is anticipating their skepticism when this was written.

However, I agree with Mr. de Fontaine Vive, we should not raise issues if they are not really big issues. So, we will take that as a lesson.

MR. CONABLE: All right. Mr. Cox.

MR. COX: Mr. Chairman, allow me to get into this discussion as well briefly.

I would hate to see staff limited in bringing to the Board's attention possible risks even though they are remote. I think this particular section of the reports are appropriate there.

I found as a lender for many years that risks rarely disappear by simply closing your eyes to them. At best, we look carefully at where the risks are and make sure that we address them appropriately as opposed to pretending that they aren't there or closing our eyes to them.

So, I take into consideration clearly what my colleague has said about why raise straw issues, issues that don't exist. And I think that is an appropriate comment. If it is a risk, bring it up; if it isn't a risk, don't put it in, don't raise it as a strawman. But for goodness sakes, I would hate for staff to take that to be that we only want selectively to raise risk issues at the Board.

I think the risk issues, as staff perceives them, should be fully put into the reports.

MR. CONABLE: I think it is a reflection of more generalized experience than it is necessarily a prediction of what is likely to happen in Rwanda.

Yes, Mr. Jaycox.

MR. JAYCOX: If I may, I would like to answer Mr. Rehm's question, or the implied question about where we stand, where we are going with respect to regional cooperation and economic integration for these landlocked countries, not only the landlocked countries but all the small economies of Africa.

In our Long-Term Perspective Study, we set out a perspective, if you will, of an increasing cooperation amongst African states on the economic front. Clearly, they are not highly complementary economies to begin with, in many

respects competitive in their export markets at least. They are certainly not competitive in their import side. And we feel that with an expanded cooperation, there can be a whole new wave of very economically justified import substitution possibilities in Africa.

Furthermore, there are all kinds of possibilities of mergers and acquisitions between companies that have been set up on too small a scale in the past and which would benefit from a wider market integration financially and in terms of corporate structure, diversification of products, specialization, all the things that lead to efficiencies in manufacturing and processing of agricultural products.

There does exist now in this part of Africa the preferential trade area, the PTA of Eastern and Southern Africa. Rwanda is a member, and all of its neighbors are members. They are in many ways finding their way at the moment.

We are trying to assist them with basically good ideas which can be the basis for international negotiation of certain new arrangements.

It is not easy to start, as I say, with competitive economies and aim toward complementary ones, where indeed the allocation of industries and so forth can be politically so

attractive that, in fact, it breaks down, that the cooperation breaks down.

But we feel that at least this PTA organization is off to a start which we can support, and hopefully we are going to be able to do that both financially as well as up till now technically.

You mentioned Pays des Grands Lac in Central Africa. This is also an entity. There are lot of these entities. In fact, there are over 100 cooperative, international cooperative entities now in Africa. Most of them are dead letters. Many of them really have no support from their membership. At least they don't pay their dues, and, as a result, they can't pay their staffs. So, they cannot function.

I think sorting out has to be done as to which one of these is worthy of development. I am not sure that outsiders can make those choices, but it is very important that we start a process whereby some kind of selectivity is fostered and indeed Africa puts forward a fewer number with greater possibilities for economic cooperation.

MR. CONABLE: Are there further follow-up questions?

Mr. Graham-Harrison.

MR. GRAHAM-HARRISON: Thank you, Mr. Chairman.

I have got a long list of points, but fortunately

they have all been addressed in the excellent responses we have had this morning from the staff and in some prior discussion. We had some concerns about, for instance, the Ministry of Capacity in relation to the open general licensing, and on coffee the need for diversification, emphasis on quality rather than expansion of acreage.

So, I am just left with the wish to welcome this project and, even though it is not perhaps strictly in order, the population project too.

Thank you.

MR. CONABLE: Thank you.

Mr. Al-Assaf.

MR. AL-ASSAF: I had a question, Mr. Chairman, that was buried somewhere. It wasn't answered about the reconciliation between the budgetary impact and the competitiveness issue.

MR. DEVAUX: The cost of petroleum has obviously an impact on the competitiveness of --

MR. CONABLE: Please speak up, Mr. Devaux.

MR. DEVAUX: Sorry. The cost of petroleum products has obviously an impact on the competitivity. You have to export coffee. There is no question about it.

On the other hand, if we want to get revenues, we

have to tax petroleum. And it is one of the easy ways to tax things and to get revenues.

Taxing petroleum does not affect the industrial sector as such, because the industrial sector is minute; it is very small.

MR. CONABLE: It is very small.

MR. DEVAUX: The only thing which it affects is the transportation of coffee and the cost of importing goods.

MR. CONABLE: Mr. Aguirre-Sacasa.

MR. AGUIRRE-SACASA: Some years ago, many years ago, in fact, we did a study, I did a study on the impact on the industrial sector of energy costs. And what we found was that of the cost structure of industry, energy costs tended to be very low, as low as 10 percent, and even lower in some cases.

What we are trying to do here in Rwanda through this policy framework and the first structural adjustment loan is to get this government and this country really to make greater use of its most abundant resource, which is its people.

One of the problems with the industrial sector right now in Rwanda is that it is very small. It is very highly protected. It has benefitted from zero tariffs on the

importation of a lot of capital goods. So, it is very capital-intensive, and it is singularly inefficient, incapable of exporting essentially.

We are trying to pursue here the setting in place of a policy framework that will allow the development of industries that will be more export-oriented, that will be more efficient, and that will be making much greater use of manpower, and where energy costs will be even lower than they are today in Rwanda.

MR. CONABLE: Mr. Al-Assaf.

MR. AL-ASSAF: Mr. Chairman, I think it was last week when we discussed the Senegal transportation sector, and it was clear at that time that the impact of the high cost of energy -- and also that was the case in other countries -- and I think, despite the small size of the industrial sector in Rwanda, I am sure it has an impact, whether it is in the industrial sector or agriculture, other products, not necessarily coffee.

So, I believe it has an impact, like other countries in Africa, and we should have a closer look at it, especially that these prices are, as I mentioned, substantially higher than international levels and neighboring countries, regional competitiveness, I think, is important here.

MR. CONABLE: Mr. Jaycox.

MR. JAYCOX: Perhaps we should go back just a little bit over the Senegal issue. In Senegal, we have an absolute crisis in competitiveness. The country cannot change its exchange rate. It has to reduce the civil service dramatically and the nominal wages eventually of all the formal sector. It has to also reduce the prices of every kind of input to industrial activity in order to become competitive if it cannot change its exchange rate.

And in so doing, it is going to forego some of the major receipts. Now, we do not advocate this point of view for a country that does have the flexibility. We find that what I am talking about has a highly deflationary effect on the economy in many cases, and it is a very, very difficult, most difficult course of structural adjustment.

In Rwanda we don't have this problem, but we need the revenues. This economy will not be able to be stabilized without these revenues.

There aren't any other sources of revenues. This is a very small economy. Its coffee and imports have to pay for everything -- schools, clinics, everything. And if they are not available, then they run deficits. And if they run deficits, then they have to continuously devalue their

currency.

So, we don't have all these options. I think the balances that have been taken in the case -- I mean, obviously we are not going to so tax petroleum that we put productive enterprises out of business; obviously not.

We are not going to tax exports of anything to the extent that we somehow can inhibit one bag of exportable coffee to leave the country. That is not the objective. The objective is to balance these things, get the revenues and get the productive activity.

I don't know if we need input from the IMF, but I mean these are the kind of considerations that go into these recommendations. We don't just go after revenue in a blind feeding frenzy. Obviously, where we go for it depends on what kind of economic impact it has.

MR. CONABLE: Mr. Al-Assaf is afraid you are going after it in a blind fueling frenzy.

(Laughter.)

MR. CONABLE: I think it is a matter of keeping a perspective and considering alternatives.

Mr. Aguirre-Sacasa, do you want to say something further?

MR. AGUIRRE-SACASA: Just two small additional

points.

On the amount of remuneration in effect paid to the Rwandan small coffee producer, we estimate that it is about 75 percent of the world market price even after the taxes that are paid. So, this is one of the highest retention rates, if you will, of any country.

MR. CONABLE: In Africa.

MR. AGUIRRE-SACASA: In fact, one of the big problems that we have had in Rwanda all along is that the producer price for coffee in Rwanda has been very high, and there has actually been a subsidy from the government to the coffee producer.

On the gasoline or petroleum derivative prices, at today's exchange rate a gallon of high test gasoline in Kigali retails for about $3.80. It is lower than in many European countries, and when you consider the distance from Mombasa and from Dar es Salaam, the ports from which this gasoline is brought, it is not, in our view, excessively high.

MR. CONABLE: All right. I don't think Mr. Al-Assaf is going to agree with you easily on this.

(Laughter.)

MR. CONABLE: But his point of view has been carefully expressed.

Are there further comments or questions?

(No response.)

MR. CONABLE: If not, the minutes will show the Executive Directors approve the credit on the terms proposed.

[redacted]