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CLASSIFICATION:

AGENCY FOR INTERNATIONAL DEVELOPMENT

PROGRAM ASSISTANCE APPROVAL DOCUMENT (PAAD)

1. PAAD Number
Grant No. 650-K-609

2. Country
Republic of Sudan

3. Category
Commodity Financing - Standard Procedure 650-K-609

4. Date
May 21, 1986

5. To
Mark L. Edelman
Assistant Administrator of Africa

6. OYB Change Number
None Applicable

7. From
Lawrence E. Saiers
Deputy Assistant Administrator

8. OYB Increase
None
To be taken from:
ESF

9. Approval Requested for Commitment of
$ $10 Million

10. Appropriation Budget Plan Code
ESF GESA-86-31650-KG32 (637-61-650-00-59-61)

11. Type Funding
☐ Loan ☒ Grant

12. Local Currency Arrangement
☐ Informal ☒ Formal ☐ None

13. Estimated Delivery Period
June 1, 1986-May 31, 1987

14. Transaction Eligibility Date
June 1, 1986

15. Commodities Financed Commodities declared eligible under the A.I.D Commodity Eligibility Listing (1978 as revised) will be eligible for A.I.D financing. NOTE: Latest revision - TM 15:89 January 1, 1986

16. Permitted Source		17. Estimated Source	
U.S. only		U.S.	
Limited F.W.		Industrialized Countries	
Free World	$10,000,000 (Code 935)	Local	$10,000,000
Cash		Other	

18. Summary Description This grant represents U.S. assistance to Sudan being made available to the Government of the Republic of Sudan (GOS) to help overcome a serious balance of payments problem.

The proposed grant will provide foreign exchange for essential petroleum imports to be agreed upon by the GOS and AID.

A grant to the Government of the Republic of the Sudan is hereby authorized in the amount of $10 million for financing the items described above, subject to the following terms and conditions:

1. Procurement will be restricted to AID Geographic Code 935 sources and Sudanese flag vessels will be eligible for ocean freight,
2. Such other terms and conditions as USAID may deem advisable.

19. Clearances	Date
AFR/PD LHAUSMAN	6/1/86
AFR/DP JPATTERSON	5-30-86
GC/AFR MAKLEINJAN	5-30-86
PPC/PB HHANDLER	5-30-86
AFR/EA SMINTZ	5/30/86
SER/OP/OS/AFR SDean (draft)	5/30/86
M/FM CChristensen	6-20-86

20. Action
☒ APPROVED ☐ DISAPPROVED

Authorized Signature: Mark L. Edelman
Date: 6/20/86

Title
ASSISTANT ADMINISTRATOR/AFRICA

CLASSIFICATION:

ACTION MEMORANDUM FOR THE ASSISTANT ADMINISTRATOR FOR AFRICA

FROM: AFR/PD, Laurence Hausman

SUBJECT: Sudan Petroleum Commodity Import Program (650-K-609)

Problem: Your approval is required for a Non-Project Assistance grant to the Government of the Republic of Sudan (GOS) in the amount of $10 million from FY 1986 Economic Support Funds for a Petroleum Commodity Import Program (CIP), 650-K-609 . The entire amount should be obligated in June 1986.

Background: On May 11, 1986, AID/AFR staff met with State AS/AFR to determine what type of assistance might be provided to Sudan in time to represent a demonstration of support for the newly elected democratic government, while at the same time recognizing USAID's lack of personnel to execute most types of assistance programs.

Agreement between A.I.D. and State was reached reactivating the idea of a petroleum CIP and modifying it to meet the current personnel and program constraints.

Discussion. In 1984, AID approved the first Petroleum Initiative CIP for $ 40 million which was followed shortly afterwards by a second grant of $40 million from FY 1985 funds. Together with $5 million in Dutch financing and $ 60 million in-kind of Saudi crude, as well as sporadic contributions by the GOS of about $8 million, sufficient supply was mobilized to get Sudan through the economically depressed, drought-stricken year.

With a more regular supply of fuel established, road transport costs were reduced by 15 percent on average, long and politically unpopular queues at filling stations were eliminated and electrical power supply became more widely available and less erratic.

Substantial progress was also made in the tendering process. The very return to the use of international competition reduced costs of petroleum to Sudan by about 30 percent. And as each tender has passed, these price advantages have become greater with tenders put out in a more timely fashion and issued to a larger number of prequalified suppliers.

The GOS made its last extensive revision of petroleum prices in March of 1985 when all fuel prices were substantially increased. In June, when the next quarterly price review was to be undertaken, strong pressure by various interest groups was placed on the Ministry of Finance to reduce fuel prices based larely on the notion that this would somehow reduce the cost of transporting emergency food assistance supplies. In June, diesel prices were also reduced by 21 percent. However, it was a move with little solid support within the GOS, and prices were restored to their original levels in 1986. With world prices coming down for most petroleum products, much of the subsidy in Sudan's pricing structure, present at the onset of the Petroleum initiative, has been reduced although the process and reasoning behind pricing considerations need considerable attention in the future.

On May 19, 1986, USAID advised us that the GOS estimates that its petroleum supply will last only until June 1st for gas oil (diesel) and June 18th to 24 for gasoline, creating a possible shortage before new sources of petroleum can be received.

Conditions Precedent:

The standard CP's pertaining to the Attorney General's opinion and the list of representatives will be included in the Grant Agreement.

Covenants.

This Commodity Grant will include no covenants.

The CIP with its allocation for petroleum was included in the FY 1986 Congressional Presentation, Annex I, Africa, on page 437. No CN is necessary.

In light of GOS progress in petroleum reform such as competitive procurement and import parity pricing, and in view of the need, the ECPR determined that AID would be justified in providing this CIP as suggested by STATE.

Sudanese local currencies generated from this CIP will be utilized for development projects supportive of AID's assistance strategy. A portion of the local currency generations will be deposited in a Trust Fund account to support Mission operations in Sudan.

Section 203 of the International Security and Development Cooperation Act of 1981 requires that at least 15 percent of ESF funds made available each year for CIPs be used to finance the procurement of agricultural commodities or agricultural related products which are of U.S. origin. The petroleum portion of the FY 1986 CIP will not meet this requirement, but the balance of the FY 1986 Sudan CIP will include procurement to comply with the provision for the program as a whole.

The PAAD (Annex A) contains an Initial Environmental Examination which recommends a negative determination for this activity. The Africa Bureau Environmental Officer concurs with the recommendation.

Mission management responsibilities have been changed somewhat from the Petroleum Initiative PAADs which the Administrator previously authorized due to the unexpected and dramatic reduction of personnel at USAID Sudan. For this PAAD, the Commodity Management Officer will have entire project management responsibilities until the personnel situation permits otherwise. The ECPR determined that this approach was feasible and acceptable.

The FY 1986 PAAD requires a Source Origin/Waiver to allow procurement of petroleum products and commodity related services from AID geographic Code 935, which would include Sudanese flag vessels eligible for ocean freight. Procurement from Libya will be excluded. This waiver is being approved by the Administrator as required.

Recommendation: That you sign the attached PAAD, thereby authorizing a petroleum NPA grant to Sudan in the amount of $10 million.

Clearances:

GC/AFR, MA Kleinjan ______ Date ______
PPC/PDPR, HHandler (draft) Date 5/30/86
AFR/PD/EAP, WWeinstein (draft) Date 5/23/86
AFR/PD, THarris ______ Date 5/30/86
AFR/DP, JPatterson ______ Date 5/30/86
AFR/EA, SMintz (draft) 5/29 Date 5/30/86
SER/AAM, SDean (draft) Date 5/30/86
AFR/CONT, TRattan ______ Date 5/30
DAA/AFR. E.L. Saiers 6/2/86

Doc. 2566J

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SUDAN

PROGRAM ASSISTANCE APPROVAL DOCUMENT (PAAD)

PETROLEUM COMMODITY IMPORT PROGRAM (CIP) GRANT

650-K-609

USAID/SUDAN
Khartoum, Sudan

May 21, 1986

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I. SUMMARY AND RECOMMENDATIONS

Throughout the 1960s, Sudan's current account was in balance or surplus. Government savings, the difference between current revenues and expenditures, were about two percent of GDP. Sudan's inflation rate and debt service were low. The economy was characterized by financial stability and private sector orientation but little growth.

Spurred by the infusion of oil-producing countries' funds and Sudan's dream of becoming the breadbasket of the Arab World, the Government of Sudan (GOS) launched a major investment program. This overly ambitious program was characterized by inadequate planning and management and ineffective public implementation and administration. The ensuing rapid growth and ill-advised economic policies stimulated a surge in expensive imported production inputs, and worse, in escalating consumption. The resulting imbalance between import outlays and export receipts widened. To cover the widening gap, the GOS resorted to external borrowing. At the same time, squeezed out of this new public sector thrust, private saving rates declined. And as the GOS attempted to subsidize consumption during the investment program, public saving rates declined as well. The growing budget imbalances which triggered increased Bank of Sudan borrowing, coupled with the external payments and debt problems, resulted in accelerating inflation and rapidly rising debt service obligations. External debt came due before physical assets achieved any production outputs. The result has been economic stagnation and staggering debt, combined with a spiraling financial crisis.

Petroleum has played a particularly crucial role in the course of Sudan's economic crisis. The petroleum-intensive irrigation and agro-industrial sectors faced collapse as world prices for petroleum skyrocketed by a coefficient of 10 from 1970 to early 1986. The new-found wealth of Sudan's oil-producing neighbors was also a two-edged sword for Sudan. On the positive side, the oil-producing nations encouraged massive investments in Sudan and its public investment program as the future breadbasket of the Arab World. On the negative side, production input costs skyrocketed, and the high salaries in Gulf states for talented managerial and technical cadres stripped Sudan of a basically competent manpower base. As of 1984, at least 600,000, and possibly as many as one million, skilled Sudanese have emigrated to take advantage of these highly attractive salaries.

Today, Sudan faces formidable obstacles in procuring petroleum supplies. Financing oil imports is one of the GOS's most critical problems as annual trade deficits have made the allocation of scarce foreign exchange difficult and imperfect. There is often the inclination to shave portions of the enormous petroleum bill in order to meet other expenses. And noneconomic considerations inevitably intervene to further distort foreign exchange allocations.

As with the rest of the economy, Sudan has dealt with its petroleum problem by means of suppressive Government control and ad-hoc and often high-handed decision-making. Domestically, the Government attempts to control

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petroleum consumption through rationing and geographic allocations while holding retail product prices below world levels. Shortages occur and the black market flourishes. Recurrent supply interruptions and shortages lead to production losses in industry and agriculture, further reducing exports.

As with the management of the rest of the economy, the importation of petroleum had become a hand-to-mouth business prior to establishment of a donor petroleum financing mechanism led by AID. USAID and the IMF estimated that the direct cost to the Sudanese balance of payments of using high-cost suppliers had been between $60 million and $100 million a year. The cost of irregular supply in terms of lost industrial production, reduced agricultural output, underutilized capacity and damaged capital equipment exceeded another $100 million annually.

USAID's approach, endorsed since 1983 by consecutive Consultative Group -- which have included Sudan -- is that balance of payments support and stabilization efforts cannot ignore the virtual hemorrhaging of the petroleum account. But getting Sudan untangled from this intricate and costly ad hoc system has been, and will continue to be, a difficult and complicated task. A cooperative effort is called for from GOS decision-makers, foreign project administrators and donors.

The initial requirement was to move Sudan back to competitive international procurement and to the extent that crude or product is not provided by donors on an in-kind basis, this objective has basically been achieved through careful tender procedures. As a result, Sudan now pays competitive prices for its fuel.

Sudan's commitment has heretofore been satisfactory. Sudan's petroleum Initiative has represented a strong revalidation of the need for, and likely impact of, resolving Sudan's petroleum mismanagement. The demands of the drought, Sudan's worse than predicted foreign exchange situation, and reduced donor interest in Sudan's regular recovery program dictate a continued USG effort to provide support through a Petroleum CIP. The need for a sustained supply of this commodity vital to the economy is essential to assure a sound economic basis for this new, democratically installed government.

With petroleum supplies assured, losses caused by fuel shortages in industry and agriculture will again be substantially reduced. And as petroleum supplies increase and distribution improves, production costs stabilize in Sudan's outlying regions, which now suffer the severest fuel shortages and rely most heavily on the black market. Conversely, without dramatic and immediate changes in the petroleum sector, stabilization and recovery will not be achievable.

RECOMMENDATIONS

The conclusions and recommendations of the CIP Evaluation, as well as the analysis made for the FY 1985 CIP, encourage the targeting of commodities most critically needed for Sudan's economic stabilization and recovery. The Petroleum CIP is an integral part not only of USAID's endeavor to achieve foreign exchange relief, but also of the overall recovery and stabilization efforts. In light of the documented need for immediate imports of petroleum products in time for the planting season, (of Sudan's percent performance in achieving targets of reform in the petroleum sector) and the importance of demonstrating U.S. continued support for Sudan especially since installation of the newly elected democratic government, it is recommended that the Assistant Administrator authorize a $10 million grant for the Petroleum CIP.

1) waiver of requirements for the Supplier's Certificate (Form AID 282) and the post audit of transactions for the Conditional Letter of Commitment and 2) authorize a source/origin waiver from Code 941 to Code 935 to allow the procurement of petroleum products and commodity-related services and ocean freight.

Editing Footnote

This document describes the volatility and erratic behavior of Sudan's free foreign exchange market for the Sudanese pound. During the development of this PAAD, the shadow price of the Sudanese pound has vacillated almost daily over the range between LS 3.3 = $1.00 and LS 4.75 = $1.00. Editing the entire document is never simultaneous and cannot keep up with the vacillations of the Sudanese pound. Thus, the reader will continually find minor variations in assumptions of the free market price of the Sudanese pound during calculations of illustrative petroleum pricing formulae.

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II. ECONOMIC CONTEXT

A. Introduction

Despite the return of sufficient rains to produce a 4 million ton grain harvest in 1985, Sudan's economy continues to be plagued by the cycle of debt, inflation and distortionary economic policies that have characterized it for years. Though fewer Sudanese may go hungry in 1986, exports will gain little over 1985. Though livestock exports remain a small bulwork, they too have been affected by drought, and the cotton crop -- which previously led foreign exchange earnings -- is again of very poor quality. Naturally the extreme scarcity of foreign exchange depresses the level of possible imports sorely needed to maintain agricultural and industrial productivity.

A new government has been elected and will assuredly find themselves again confronting key economic policy issues on foreign exchange rates, the import administration, farmgate and exporter agricultural prices, consumer prices, and monetary growth as they seek to restore productivity. The agricultural price structure continues to create disincentives to both overall production and to exports, and official consumer prices still stimulate consumption beyond supply availability. Furthermore, Sudan's relationship with the IMF has not yet been re-established; no Stand-by agreement is in place and negotiations to achieve one have not commenced. Without a Standby, Sudan is limited in the amount of donors financial support and debt rescheduling achievable for 1986. Debt arrearage will mount beyond current levels, which already threaten to completely absorb annual export inflows, and donors cannot be expected to greatly alleviate constraints on imports. The GOS itself has been unable to reduce expenditures or raise revenues sufficiently to reduce a massive budget deficit. Since the central government tax structure is primarily trade-based, we do not expect any major deficit reductions this year, a post-election year, in which expenditure reductions may prove politically infeasible.

B. Performance Indicators

1. Trade Deficit

In Sudan, the 1985 trade deficit (while still a staggering +25% of GDP) has eased if only due to the lack of resources to continue recent levels of imports. Exports were no more than $300 million, while imports remained over $1.3 billion. Clearly there is still a foreign exchange supply, in addition to official exports, coming in as remittances from Sudanese working abroad and unofficial exports which acts to cover the trade gap exceeding $600 million left by low domestic productivity. Donors too have cushioned the import financing needs of the stricken Sudanese economy. Without donor assistance the gap would have been wider by at least $300 million, due to wheat and petroleum financing requirements.

Exports:

Recent estimates of Sudan's export earnings for 1985 are projected at no more than $300 million. In real terms it shows export production to have fallen off badly since the late 1970's. Drought conditions persisted until the last half of 1985, which combined with weak international demand, unfavorable export prices and implicit GOS taxation of exporters, has strangled exports. The drought of the last two years caused severe damage to agricultural production overall but was particularly felt by Sudan's vibrant rainfed sector from which comes groundnuts, sesame, sorghum, and gum arabic for export.

In 1984 and again in 1985 the export market for Sudan's sorghum was inhibited both by falling international prices and very high, scarcity-related domestic prices. The exportation really only re-emerged at the end of 1985 but was inhibited by export restrictions aimed at domestic food security.

Sudan faced severe problems exporting cotton in 1985. At about 726,000 bales, the volume was 25% less than 1984 and 35% less than 1983, none of which were banner years for Sudanese cotton exports anyway. To begin with, cotton production has suffered in terms of both quantity and quality from excess government control of irrigated schemes, including implicit taxation of cotton producers of at least 33%. Moreover, the parastatal Cotton Marketing Board has failed to aggressively market its available cotton (much of it severely damaged by white fly infestation) to maximize revenue in a very competitive cotton market, where international prices are falling due to production increases. The best Sudan could have hoped for, in any case, was to minimize revenue losses given the fall in nominal medium staple cotton prices from US 70¢/lb. in January 1984 to US 48.5¢/lb in October 1985.

Sudan's pre-eminent position as a supplier of gum arabic to the world market has suffered a strong blow in 1985. Exports in 1985, estimated at about 23000 MT are approximately down by 40% from levels of 1983 and 1984. Moreover, Sudan had to draw its domestic stocks down completely just to maintain this extremely low export level. For 1986, producer auction floor prices were finally raised by 80%, while in 1985 it was still far more profitable to cut gum-producing trees for sale as firewood. Sudan has already lost part of its gum market to readily available substitutes or aggressive international competitors such as Senegal. We are hoping for some recovery in 1986 in response to price incentives.

Sudan's groundnut exports, which were 108,000 MT and 18% of total export value in their most recent peak of 1981/82, were modest in 1985 at around 12,000 MT and around 2% of export earnings. Sudan's domestic production has fallen drastically in recent years, by over 50% since the early 1980's. This, combined with associated soaring domestic prices and concurrent recent declines in world prices has reduced groundnut export earnings to just about $6-7 million.

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2. External Debt

Sudan's external debt has grown further to the staggering sum of over $10 billion, which in nominal terms is about 20 times Sudan's annual official exports. The annual debt service obligations of the country well exceed $1 billion which, about triple recent annual export earnings. There is clearly no way that Sudan can finance such a debt without some combination of massive donor assistance, mounting arrears, extremely liberal rescheduling agreements, and rapid increases in money supply (a consequent high inflation rates). In recent years, Sudan's recipe for staving off bankruptcy has included healthy proportions of each. What is has not been successful in doing is combining export growth and import demand management to ease the burden somewhat.

As of September 1985, Sudan was in arrears on approximately $1.241 billion in principle payments and $446 million in interest payments on loans from various multilateral, bilateral, commercial bank and supplier sources. Obligations for fiscal year 1985 total $742 million and $525 in principal and interest respectively. Most expect genet..s rescheduling of most of it, given the very low probability of repayment and the realization that Sudan cannot achieve growth under such monumental financial stress.

3. Government Budget Deficit

Even excluding external debt obligations, the GOS budget deficit would exceed LS 1 billion in FY 1985/86. In fact, estimates are of a LS 1.2 billion deficit for the period, fueled to a large extent by defense spending exceeding 25% of current expenditures in the entire budget. This is, of course, related to the civil strife between the North and the South, but also to the development of localized public flare-ups and the potential for more as scheduled elections draw near. The current estimated total budget needs by the central government alone is approximately LS 2.75 billion, some +25% of estimated GDP. Central government revenues are estimated at about Ls 1.5 billion (about 14% of GDP). Taxes on trade at Ls 745 million (mostly on imports) are more than double those on income and profits in Sudan. The country still has no real broad-based income tax, and no domestic consumption tax per se. There is a great popular reluctance to participate in such taxes, in any case, given the paucity and deterioration of basic public services. Local currency generations from donor provided commodities has occasionally helped fill the financial void in recent years. Without real expenditure reduction and re-orientation, i.e. toward public goods like education and economic infrastructure, the budget deficit is unlikely to become much less severe in the next year to two.

4. Money, Credit, and Inflation

There is little doubt regarding the relationship of the rapid expansion of money supply generally, which in Sudan is to a great extent achieved by credit expansion, and the associated price inflation which follows. Given the tremendous twin burdens of the GOS budget deficit and external debt, the pressure to expand money supply is close to irresistible.

Sudan has always had trouble meeting the target's for monetary expansion agreed to with the IMF. Recently, mounting political demands by various public sector trade, unions, the continuance of North-South civil strife, and mounting pressure for increased consumer subsidies rendered the GOS completely out of conformance with the target.

Money supply growth (as calculated by the GOS and IMF staff) was around LS 575 million for the 3 months of October through December 1985 alone, when the total projected change for fiscal year 1985/86 was LS1.061 billion. The GOS was already expanding twice as fast as planned. The major snag was GOS credit, which though targeted to increase by LS 225 million for the entire fiscal year, grew by LS 286.3 million in this 3 month period alone. Notably, this is over 7 times the rate (in nominal terms) of expansion recorded for the same period in 1984. Credit to so-called public entities (or parastatals) was also running far ahead of targeted growth. Growth, at LS 174.3 million for the 3 month period, was more than double that suggested by the projected fiscal year 1985/86 target of LS 294 million. Not surprisingly, a "go-slow" approach to private sector credit made up a small bit of the difference, expanding by half of its targeted rate of LS 73 million for the period. Private banking credit grew by just LS 36.5 million from October through December 1985.

As the money supply grew by about 10% for this three month periods, prices too continued their overall upward movement. In 1984/85, in fact, it appears that drought-related supply scarcity was partly to blame for prices growing by well over 60% while money supply grew by about 49%. In 1985/86 production increases have already mitigated critically high sorghum prices. Inflation, it is hoped will be less this year, but undoubtedly will exceed 35% as Sudan's economic low productivity and financing woes exacerbate scarcities. A great deal will depend however, on GOS ability to curb it's resort to excessive money supply expansion to meet short-term crises.

5. External Financial Resources

Sudan's two main sources of foreign exchange aside from export earnings and earnings and savings from debt rescheduling, are donor assistance and remittances. Donors rallied to Sudan's cause in the last two years, when the lives of large segments of the population were threatened by drought. In 1984 donors committed about $735 million total for balance of payments support and projects. In 1985, drought relief assistance totalled $ 200 million and other types of assistance (balance of payments and projects) totalled over $ 200 million.

6. Gross Domestic Product

In real terms GDP has been in decline since 1981/82, when Sudan had a bumper crop harvest. Although the economy enjoys an exceptionally important service sector given low per capita incomes (about 50% of GDP at market prices) much of it is related to agricultural marketing, though a significant portion are public services. The fate of the economy is clearly tied to that of the agricultural sector. When rainfed production falls, as it has during recent severe drought conditions, GDP usually declines. 1985 was no exception. Despite improved rainfall in the latter half of the year, its production benefits will be felt in 1986. At market prices, 1985 GDP was about LS 10.6 million but was down about 1.5% from 1984's levels in real terms. We expect improvements in 1986 given agricultural production recovery. Given Sudan's annual population grow rate of approximately 2.8% annually, however, the country will face great difficulty maintaining real per capita production levels.

C. 1985 Developments:

1. Drought Impact, Recovery and Rehabilitation Prospects

Overshadowing and exacerbating the strain on the Government resulting from the civil war in the South and the transition of power in the Central Government, is Sudan's drought.

When the rains failed again in 1984, the GOS and the donor community faced the specter of over 7 million people starving to death across Sudan. Since then USAID and the other donors have channeled scarce development resources into the most massive famine relief effort ever undertaken.

The United States alone spent millions of dollars and Sudanese Pounds (from counterpart fund accounts) on the relief effort. Over 500,000 MT of Title II foods representing about 85% of total donor food aid in 1985 were delivered to Port Sudan for distribution in both the Eastern and Western Regions of the country. However, distribution of such large quantities of food to remote areas of Sudan, difficult under the best of circumstances, proved to be an almost impossible task in 1985; torrential rains swept away both the rail line and inundated the roads creating huge lakes which virtually cut off entire populations from the life-saving food being delivered by truck. By August 1985, the situation had deteriorated further and the US and the EEC launched tandem airlifts to move food and fuel to Darfur region in the West.

While the rains stymied the famine relief effort, they were welcomed by the farmers. Responding to existing high market prices for grain, farmers throughout Sudan not only moved from cash crop production to food crop production but also expanded total acreage under production beyond any previous levels in recorded history. The result by December 1985 was a harvest of over 4 million tons of grain, more than one million tons above the estimated food and storage needs for the entire country.

Despite the overall grain surplus, there are areas of Sudan which had little or no rainfall and others which were heavily infested by desert locusts. In these areas, some 3.5 million people are believed to face malnutrition and even starvation once again if assistance is not provided. The majority of those thus affected this year reside in the Western Regions of

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Livestock exports have played an increasing role in Sudan's export earnings, moving from about 8% of official earnings to about 24% in 1985. Unfortunately, however, aggregate revenue in 1985 has fallen to about $82 mil from 1983's high of about $122 million. The number of head exported is, however, little changed, as some international livestock prices fell. During the last two years, drought conditions enhanced the willingness of livestock owners to sell off their herds because the feeding costs increased dramatically. It will take at least two or three years to rebuild these herds and the numbers exported are not expected to match 1985 levels in 1986 or 1987.

Sesame exports have strengthened since 1979 in response to rising international prices and production increases due to area increases. The drought, however had a negative impact on the 1985 sesame export revenues. At a projected $37.5 mil, they are down from 1984 by more than a third. The production is expected to recover somewhat in 1986 with the onset of more typical rainfall patterns and export revenues will then show clear increase given sesame's growing world prices.

In 1986 Sudan's agricultural exports should partially recover, particularly those from rainfed areas where production costs are relatively lower than in irrigated schemes. The main obstacles will be fast increasing real production costs, particularly as international prices grow more slowly or even decline, and the tendency of the GOS to implicity tax exporters and export producers by applying an overvalued exchange rate to determine prices they can receive for their goods. There are many other policy issues, such as the poor effort of the GOS in marketing cotton, which will act as constraints to export production. We are particularly concerned about recent announcements regarding the possibility of reintroduction of a public oilseeds monopoly and a GOS incursion into the livestock/meat marketing sector designed to cut consumer meat prices but with an inevitably negative effect on livestock exports and eventually on production. In short, we expect continued macroeconomic distortions to hamper export-led growth tactics.

<u>Imports</u>

Sudan's import financing requirements for 1985 were significantly reduced due to massive donor assistance in food and petroleum importation. The value of the import portion of the assistance totalled approximately $ 340 million. Nonetheless, the final official import bill for 1985 was not less than $1.3 billion. It was mainly comprised of consumption goods such as petroleum, wheat and wheat flour, agricultural chemicals, foodstuff and pharmaceuticals, with smaller amounts for more durable items like machinery and vehicles, but with little in the way of contribution to fixed capital investment. This is an unsurprising pattern given the poor investment climate, high inflation rates, the relatively low living standards of the population, and seemingly skewed income distribution. Sudan's economy is biased towards consumption in many ways, and import demand is expected to continue strong. This is especially true given the economic peculiarity of having a large share of the country's skilled and semi-skilled workers abroad and remitting substantial sums to Sudan.

North Darfur, North Kordofan, and the Red Sea Hills Provinces. Less affected yet still requiring substantial assistance are populations in the Central Region and Northern Kassala Province. These figures do not include the unknown thousands in Southern Sudan who face starvation as a result of the on-going civil war in that area.

The donor community has established that 400,000 MT of cereals and supplementary foods are needed in 1986 to respond to the continuing crisis in the Northern areas. The security situation in the South is such that food aid on a massive scale cannot be considered at this time. It is well-recognized, however that Southern food needs are very serious. In 1986, the US will provide 200,000 MT of sorghum and supplementary foods, one half of the total food aid program. Major responsibility for implementing USAID's drought relief program has been given to the PVOs, as USAID views this year as a transition year from emergency assistance to rehabilitation in affected areas. The PVOs gained experience in Sudan drought relief in 1985, and have the management skills required to implement this year's targetted program. USAID hopes to focus its attention on long term planning.

In order not to dampen future production incentives and taking into account the neglible purchasing power of drought affected people in the West, donors devised a new food aid strategy which responded to the anomaly of pockets of food deficits in a food surplus economy. Rather than importing food aid, the US and other donors purchased almost 100,000 MT of local sorghum through open tendering and private negotiations with local merchants. This grain is being redistributed in deficit areas, primarily Northern Darfur and Northern Kordofan by PVOs working in those areas.

In this year of transition from famine disaster to recovery, food aid alone is not sufficient. Years of drought have left millions of people with neither livestock nor savings. Many people have moved to new areas hoping to rebuild their lives. Most are overburdened with debts which thoy cannot repay. Donors are responding with a series of programs aimed at restoring the quality of life and the economic viability of some of the drought affected areas and increasing the services in those areas which have received an influx of migrants. Water yard rehabilitation and intensive child survival programs are only two of the activities supported by both donors and the GOS to initiate this process. Longer term strategies are being devised which address the need for credit, for the revitalization of small businesses and for education and training.

Given the tremendous size and diversity of Sudan, USAID is designing policies and programs which will help to strengthen the ability of individuals and communities to become more self-sufficient. A first step in this direction must be food security. Towards this end, USAID hopes to begin activities which will contribute to long-run food security such as improved and decentralized grain storage and the multiplication of high yielding hybrid sorghum seeds. Beyond our control but critical to the success of this food security strategy is the continuation of sufficient rains. For this year, at least, the return of the rains has eased the pressure to feed millions of people. With a reduced food assistance program which emphasizes the role of the PVO as program implementer, USAID has somewhat freed itself from full time drought relief management and has begun to turn its attention towards activities which will help prevent the recurrence of last year's near tragedy, those that contribute to longer run growth and real development.

2. Political Transition - Effect on Reform Environment

In May elected officials began to form a new government, which is a lopsided coalition of parties. The Umma Party headed by Sadig El Mahdi, the new Prime Minister, has the greatest number of seats and influence, and has effectively managed to form a cabinet wherein Southerners and Unionists are significantly represented but in which the National Islamic Front plays little role. The ability of the government to implement economic reforms depends on the strength of this coalition and cabinet.

The Umma Party political economic platform focuses on improving the standard of living for the poor, the use of centralized planning in managing the economy, increased investment, and prevention of capital flight and "braindrain." The party has previously suggested tax reformation, rehabilitation of existing industrial and agricultural concerns, debt rescheduling, import demand control, policies to increase remittances, reaching a one year agreement with the trade unions on consumer prices, supply food storage and small farmer seeds and credit through the public sector, improve public service delivery, and reform the banking system to allow a return on capital lent and to allow the private sector to focus on capital investment lending while the public sector provides commercial credit. In addition, they will seek to maintain rural producer prices. Although clearly the public sector is to lead an economic recovery, parastatal activity which conflicts with private production will apparently be reduced, and foreign investment and private cooperatives will be encouraged, the Umma Party recognizes the economic importance of the rainfed agricultural sector and has a stated commitment to reform in the interest of the producers. There is also a clear intent to protect local industries and develop new ones. The Umma Party rightfully recognizes that to do this, consumer prices must cover producer costs and reasonable profits.

It remains to be seen which of these Umma Party priorities will be included in those of the coalition government. Despite the very expansive role that seems to be planned for the public sector, there are apparently many good options for policy reform.

Since the April coup in Sudan newly appointed high level officials whose term of office was not expected to last more than one year, until elections, have been reluctant to undertake difficult policy reform measures. In fact, they have been much more receptive to demands from various political groups, whose demands are now much more highly publicized via a liberalized media and newly registered political parties. The trade unions are particularly influential in this process. Not surprisingly, there have been calls to ease the burden of price inflation from vocal groups. The Nimeiri regime itself attempted to stave off opposition by reducing retail bread prices from 18 to 15 piastres. Following the coup, in June 1985, gasoil prices were reduced from LS 3.5/gallon to LS 2.75/gallon and precipitated an annual revenue loss of LS 150 million. Thereafter, as we have mentioned elsewhere, tenets of an IMF reform program were systematically circumvented. In recent days, just prior to elections, the newly instally time Minister of Finance had promised further relief from high prices, and has systematically set upon urban Khartoum shopkeepers who are "smuggling" food items into the country, i.e. using foreign exchange purchased in the free market to purchase imports, and subsequently pricing them accordingly. Such prices exceed officially controlled prices and merchants are thus being blamed for inflation. Some have been jailed and other risk having their "smuggled" items confiscated for sale through public entities. In addition drought related herd reductions has resulted in rapidly increasing meat prices in Sudan. The GOS, after publically fingering those involved in livestock marketing for the increase has recently announced a policy of public intervention in meat markets to slow exports and procure meat to sell at subsidized prices.

Finally, the GOS announced new policies related to the foreign exchange market in February 1985. Foreign exchange accounts are to be centralized under the control of the Foreign Exchange Committee, a newly created entity. Commercial bank private customers will no longer be allowed to use the accounts for private importation after January 1986. Imports are to be much more tightly controlled hereafter. In addition, the restrictions placed on foreign exchange accounts and foreign exchange uses will constrain the ability of the Sudanese to use remittances for imports through the free markets. It intends to drive remittances into the bank. The outcome is likely to be fewer gross remittances and consumer good imports overall. The commercial bank foreign exchange rate itself is ostensibly still to be flexible, i.e. to act as an incentive to use the banking system, but has not in the last year operated as such.

In sum, we do not expect any tough reform decisions to be taken in the foreseeable future and do not believe the newly elected government will relish the opportunity either. Most recent macroeconomic reforms have involved increasingly centralized market control and consumer subsidization. This is not the preferred approach from USAID's point of view.

Sectoral reforms, especially related to maintaining producer price incentives have been much more positive. Wheat and gum arabic prices have been increased substantially in 1985/86 to encourage production. We expect sectoral reform and local initiatives to continue relatively less restricted.

3. The South

The Central Government remains embroiled in a costly and destabilizing civil war prosecuted against Southern Sudanese rebels. Not only does the failure to achieve a settlement of North-South differences threaten chances for a stable elected government, but it exacts a heavy financial burden. Revised budget estimates for 1985/86 indicate that defense expenditures are running about 25% of the operating budget instead of 14%. Progress on domestic petroleum production is now severely delayed and will remain so until security in the South improves. The Southern region as a whole is possessed of substantial natural resources (land, water, timber) or potential economic value that languish underdeveloped, not to mention human resources, as the conflict continues.

5. <u>IMF Arrangements</u>

Sudan has been in arrears to the IMF since July 1984 when its standby arrangements collapsed over the development of $42 million in arrears. Arrears for 1985 are just over $200 million and are expected to be around $175 million in 1986. Paying them without assistance is out of the question for Sudan. Moreover, despite 17 months of discussions on an acceptable reform program, the GOS and the IMF were unable to come to any meaningful terms of agreement, in large measure due to the hesitancy on the part of the GOS to accept even the most modest proposals. In February, 1986 Sudan was formally declared ineligible for further participation in the IMF loan program which include their newly developed program of $2.7 billion for African economies.

Admittedly, over the last year and a half Sudan has gone through a radical political transition involving a coup in April 1985 the resignation of 2 finance ministers, and, finally, preparation for forthcoming elections. Nonetheless, they resulted in part from difficulties in resolving IMF issues, as much as they caused those difficulties. It is worth reviewing the general areas of policy reform that were intended to be part of an ongoing program, and the progress thereon to understand what was behind the declaration of ineligibility. They include the following objectives:

1. Commodity Price Decontrol - a list of thirty items for phased decontrol was prepared but deadlines for specifying which would be first and how the flexible price/profit setting system would work have passed unfulfilled.

2. Positive Interest Rate Adoption - No plan has been developed and no action taken despite annual inflation of perhaps over 50%.

3. Controlled Monetary Expansion - The 1985/86 target was set at 20% and after one quarter expansion was already double a rate consistent with this objective.

4. Targeted Credit Expansion - In the first quarter of 1985/86, GOS credit had already exceeded their entire years's target, parastatal credit had expanded at double the recommended rate and, unfortunately, private sector credit was half its recommended levels for the quarter.

5. Reduction of Extrabudgetary Expenditure Items - The intent was to virtually eliminate these yet the 1985/86 budget contained a 12% "reserve" for these items.

6. Raise Revenues - Soon after the ambitions revenue raising objectives of the September 1985 budget were announced, it became very clear that the GOS could not meet its target of LS 230 million in additional reserves. Certain commodity taxes and provisions for income taxes were rolled back in the face of public opposition. In addition, another LS 90 million in new revenue sources was to be identified and was not. Land and water charge increases were accepted but have yet to be implemented.

7. Commercial Bank Establishment of Flexible Foreign Exchange Rate- Neither the establishment of freely competitive rates by the banks nor the adoption of a "currency basket" approach to setting the rate has been adopted formally to achieve devaluation. Perhaps wisely, banks have developed ways of competing for foreign exchange business on a more informal basis. This is especially true as most current cabinet ministers oppose these currency devaluation attempts.

8. Import System Improvements - Despite IMF jawboning on this issue, no real changes have been made. Issuance of licenses remains somewhat haphazard and crisis-oriented.

9. Cotton Price Adjustments - Increases in procurement prices were due on December 1 and were not announced.

In sum, in all the areas of discussion and change the GOS failed to agree on the elements of the standby arrangement with the IMF. This, combined with arrears, led to Sudan's recent "ineligible" designation.

III. SUDAN'S PETROLEUM SECTOR

A. Petroleum Initiative Impacts and Progress

In 1985, Sudan's Petroleum Initiative's operation was severely tested when drought-caused reductions in exports rendered our original notions of GOS financial contributions unachievable. It turned out to be fortunate that the disbursement of 1984 petroleum funds was delayed until May of 1985 due to the difficulties inherent in implementing a very complex program for the first time. Sudan thus had $80 million in total USAID resources in CY 1985. The $5 million Dutch financing contribution and $60 million in-kind Saudi Crude shipments, 300,000 MT, were also mobilized. In addition the GOS was able to secure a commitment for 300,000 MT in crude shipments from the Libyan government, of which 150,000 MT had arrived by October 1985. Between mid-August 1985 and January 1986, the GOS even managed to put up $7-8 million itself to finance petroleum supplies, despite the severely limited foreign exchange supply.

By October 1985, black market prices in all regions of the country (except the South) had fallen 50 and 30% respectively for gasoil and benzene. Fuel is often 30% of total road transport costs. Thus, all else equal, road transport costs were reduced by 15% on average. As road transport is very widely used, many consumers and producers benefited by these supply improvements. In fact, produce merchants were publically connecting the stabilization of food prices with the improved fuel situation. The easing of the supply situation also was noticeable in the near elimination of long purchasing queues in urban areas, and the lessened amount of time and risk consumers had to bear in seeking additional supplies in the black market. Having a more regular fuel supply has also contributed to the availability of electrical power in Sudan, and to the clear reduction in outages in the Blue Nile grid area.

Under the auspices of the Initiative's competitive procurement requirements, substantial progress has also been made in the tendering process itself. The more timely use of tenders, issued to a larger number of prequalified suppliers, has allowed Sudan to obtain its supplies at highly competitive international prices. Sudan has paid about 30% higher than world market prices in recent years, so this represents a tremendous savings. In addition, the day to day planning needed to determine, timing, commodity mix and quantities under the facility is bearing fruit in terms of the institutional development of the General Petroleum Corporation (GPC), and the coordination required between the Ministries of Energy and Finance and the Bank of Sudan.

Despite the considerable progress made in the last 6 months, a number of institutional changes have yet to be made due to the April 1985 change in the national administration and subsequent naming of new Ministers of Energy and Finance, and of a new Bank of Sudan Governor and a Director of GPC. We have worked closely with the above to ensure that the basic objectives of the

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Petroleum Initiative are reiterated and that these new officials are able to consider them in developing their programs. Some of the issues we are still moving forward on include the timeliness of the tenders and their financing, the institutionalization of an Advisory Committee to the GPC including private distributors and intended to discuss importation mix and internal allocation and distribution plans. We are also continuing to focus on a revision of the internal allocation and distribution system to allow a greater market orientation.

The GOS made its last extensive revision of petroleum prices in March of 1985 when all fuel prices were substantially increased. In June, when the next quarterly price review was to be undertaken, strong pressure by various interest groups was placed on the Ministry of Finance to reduce fuel prices, based largely on the notion that this would somehow reduce the cost of transporting emergency food assistance supplies. In June, official gasoil prices were reduced by 21%. It was a move with little solid support within the GOS, however, and gasoil prices were restored to original levels in early 1986. There also commenced an official effort to raise benzene (gasoline) prices, as well. The GPC has developed a computer model of price subsidies as a basis for discussion. Despite the tenuous political environment for many officials, which precludes making bold moves on petroleum prices, the debate about proper fuel prices is very much alive and USAID/Sudan continues to play an active role in these policy discussions. We have found the discussion process itself to be a useful way of introducing our general concerns regarding the petroleum sector to recently appointed officials. Given the current public satisfaction with the increased level and regularity of petroleum supply, it may become more feasible to institute a more standardized pricing mechanism over the next year as agriculture recovers from drought, and with it the entire economy.

B. Current Requirements and Resources

Although true market demand is unknown due to financing scarcity and official prices set below market clearing levels, the minimum consumption level consistent with economic stabilization is at least 1.2 million metric tons. At current prices and consumption mix, that supply would cost about $225-250 million in the international market. To achieve real economic growth Sudan's requirements are considerably higher. The Southern and Western regions, for example, officially receive no more than 4 percent of the nation's supply despite having over 30% of its population. Most regions are similarly supply constrained, which obviously inhibits economic activity. Black market prices in these areas indicates a value being placed on available supplies of more than double import parity level prices. This is a clear indicator that customers are willing to buy considerably more fuel and could use it profitably. The National Energy Administration estimates that unconstrained demand grows about 7% annually and had previously calculated 1985 requirements at about 1.57 million metric tons. Requirements for 1986 would be about 1.68 million metric tons. Achieving that level of consumption would cost Sudan about $340 million. That probably comes close to 1986 total export earnings.

The government of Sudan is thus in a very poor position to finance even the minimum fuel supply needed by the country, much less the level needed to boost growth. From the end of October 1985, $40 million was available from 1985 USAID petroleum funds, 150,000 metric tons of crude remain from the Libyan commitment and the Bank of Sudan may come up with about $50 million in resources over the next year. So long as USAID 1986 petroleum funds become available in the 12 month period beginning in November 1985 as well, the first six months supply financing is already accounted for. Negotiations between the GOS and Saudi Arabia successfully rendered a commitment for 400,000 MT of crude; the Libyans are talking of another 300,000 MT, and Kuwait may offer some refined products. US funds from this particular CIP will cover some 50,000 tons of refined product.

Sudan's specific petroleum import requirements are shaped both by its refinery operations and by actual consumption needs. The refinery output would not produce enough gasoil, the fuel of the economy, even if fully utilized. The refinery's maximum capacity is about 1 million MT annually which falls short of total needs in any case. Sudan's supply/consumption pattern for the next 12 months will likely be similar to the following:

('000 MT)

	Imported	Refined	Total
1. Crude	750		
2. Gasoil	410	240	650.00
3. Motor Gasoline	106.25	108.75	215.00
4. Fuel Oil		206.25	206.25
1500	41.25	108.75	150.00
3500			
5. Kerosene/jet Fuel	36.25	48.75	85.00
6. Butagas	4.0	3.75	7.75
7. Losses & Refinery operations		33.75	33.75
			1.347 mil MT

This consumption level would represent an increase of about 20% over 1985 levels. Such a jump is necessitated by years of stagnation in the supply. From 1979 through 1983 annual consumption increased 2.34% on average, and actually declined from 1983 until the present. Clearly, per capita fuel availability has actually declined over the entire period. Given the well-documented relationship between rates of economic growth and rates of growth in energy supply, supply has not met economic requirements and is seriously constraining growth in Sudan.

Over the short-run, the following supply figures have been given to USAID/Sudan mission staff:

The current supply situation for each major fuel and the metric ton stock level as of May 3, 1986 is as follows, according to the General Petroleum Company (GPC):

A. Crude

-- stock	66,585 MT
-- expected imports (from Saudia)	50,000 MT

This will be sufficient up to June 14th

B. Petroleum Products:

-- LP	
-- stock	649 MT
-- expected refinery production	333 MT
-- expected imports	500 MT
-- total	1,482 MT
-- daily consumption	40 MT

This will be sufficient up to June 10th

C. Mogas (regular benzene)

-- stock	
-- expected from refinery	9,854 MT
-- total	33,850 MT
-- daily consumption	650 MT

This will be sufficient up to June 24th

D. Super Mogas (super benzene)

-- stock	772 MT
-- expected imports (from Kuwait)	2,000 MT
-- total	2,772 MT
-- daily consumption	60 MT

This will be sufficient up to June 18th

E. Jet A1

-- stock	16,088 MT
-- expected from refinery	6,000 MT
-- daily consumption	250 MT

This will be sufficient up to June 30th

F. Gas Oil

-- stock	50,700 MT
-- expected from refinery	19,975 MT
-- total	70,675 MT
-- daily consumption	2,600 MT

This is sufficient up to June 1s(

G. Fuel Oil

-- furnace 1500	
-- stock	10,293 MT
-- expected from refinery	16,380 MT
-- total	26,673 MT
-- daily consumption	1,150 MT

This is sufficient up to June 5tl

H. Furnace 3500

-- stock	29,486 MT
-- expected from refinery	10,720 MT
-- total	40,206 MT
-- daily consumption	450 MT

This is sufficient up to June 31st

As for lubricants stock and supply situation, GPC comments that lubricants supply from the Italian and Netherland grants is sufficientto the end of August.

GPC officials said that there are no shipments for the third quarter and (July, August, September) needs are not covered. They are waiting for the new minister to be appointed to come and start contacts with Arab and friendly countries to help in this matter. Meanwhile, GPC assesses the country's requirements of petroleum products for the third quarter of the year as follows:

	Third Quarter Requirements		One Month Requirements	
	Quantity (MT)	Value ($000)	Quantity (MT)	Value ($000)
Crude Oil	300,000	29,565	100,000	9,855
Gas Oil	130,000	16,575	40,000	5,100
Mogas Regular	25,000	3,975	8,000	1,272
Mogas Super	5,000	892.5	1,500	267.75
Fuel Oil (Furnace 1500)	40,000	2,840	15,000	1,065
LPG	2,500	276.25	800	88.4
TOTAL		54,123.75		17,648.15

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Foregoing prices are based on Rotterdam and the Mediterranean spot prices.

In May and June GPC usually tries to build stocks in the provinces before the rainy season to support the agriculture season. They are unable to do so this year.

C. Petroleum Sector Setting and Constraints in Sudan

Supply and Demand

Sudan's petroleum supply and demand balances are affected by decisio taken in a number of government agencies in the course of any given year Decisions to allow implicit taxation of exports (through undervalued official export prices) and to allow the Sudanese pound to become increasingly overvalued, for example constrain foreign exchange supply in the first place. The determination not to recognize the existence of the free foreign exchange market closes off another option for petroleum supplies. Consumption thus remains limited by Sudan's inability to finance the importation of adequate supplies of petroleum products. The demand for fuel in Sudan is known to be strong, given that black market prices exceed import-parity prices substantially. In the Khartoum urban area, demand is artificially increased by subsidies on consumer prices for gasoil and fuel oil (which is used in electricity and rail transport). Official prices throughout the country are supposed to be subsidized but seldom are elsewhere. Unfortunately, the revenues then accrue to middlemen, and continuation of official price subsidies insures that not enough domestic currency is collected to finance resupply in any case.

Potential petroleum demand is clearly higher than what is able to be supplied under the current regulatory structure. In 1985 Sudan consumed (with substantial donor assistance) approximately 1.14 million metric tons of fuel. Aggregate consumption has not increased since 1983, and thus per capita availability is declining by nearly 3% a year. Even should domestic production come on stream in the next few years, Sudan's trade deficit is likely to remain serious. Thus financing adequate petroleum supplies for consumption will remain problematical for the foreseeable future.

Financing

Sudan has not moved much closer to self financing petroleum despite the implementation of the Petroleum Initiative. Drought and other constraints to exports and remittances have hampered foreign exchange availability. Hence, the financing objectives we sought in earlier agreements were not achieved. In the first quarter of 1985, the private sector did respond very clearly to a liberalization of their access to petroleum import licenses. The value and volume of private imports increased by several fold over the quarter immediately prior to that. In 1985, Sudan did manage to obtain financing assistance from the Libyans and Saudis valued at up to $80 mil, in addition to USAID's $80 million in CY 1985. The GOS itself financed about $75 million worth which, if private imports are counted, is equivalent only to about 25% of total financing. During the course of the facility, the GOS has not redeveloped any substantial suppliers credit facilities with major international oil companies. For 1986, donor assistance is again needed to maintain consumption levels provided private imports are not again expanded and the foreign exchange market remains heavily restricted.

Sudan's total petroleum import bill, even assuming that lower prices hold will be around $225-250 mil for 1986. Thus, petroleum will continue as Sudan's predominant import, and a foreign exchange burden second only to external debt service obligations.

Pricing

During this year of political transition and instability, populer demands for subsidies were more loudly made and much more needed. The initial hard push to cut prices of consumer goods came in June 1985 and the petroleum sector was the loser when gasoil prices were cut 21.4%. Few but urban Khartoum and/or public sector consumers ever face such a price. Free market benzene and gasoil prices did fall thereafter, but not by administrative fiat. Rather, supply expansion and a recession-caused drop in demand were behind it. Even at todays new low international petroleum prices, Sudan's official prices for fuel oils and gasoil (or diesel) were heavily subsidized. In early 1986, the GOS reversed its gasoil price decrease and thus, now gasoil prices have only a slight subsidy at current low international prices. Benzene official prices exceed import-parity prices at the commercial bank rate and much beyond, but do not match market-clearing prices. Nonetheless, current prospects for price increases are not strong especially in the aftermath of the populer elections. Increasing prices of all petroleum products to market clearing levels, or even just to import parity would ensure enough revenues to resupply even in the face of sharp domestic inflation. It is an issue which will continue to thwart GOS efforts at financing adequate supply.

Importation

In the course of the Petroleum Initiative, Sudan has managed to achieve prices through a competitive bidding process, far closer to world market spot levels than in recent years when premiums ranged from 30-60%. The procurements have become considerably more timely and orderly, though a "crisis management" approach still prevails. Over the course of the year (1985) the GOS did develop and use fairly consistently a list of prequalified bidding companies. USAID was a close observer of the actual procedure from tendering to assessing bids and making awards. Given constrained 1985 financing levels, Sudan could not have maintained volumes at previous levels, nor this years continuity of supply, without these improved procedures for importation. We expect them to continue under the auspices of this agreement.

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Allocation

Sudan's allocation and distribution system continues to be administered by the GOS primarily through the General Petroleum Corporation. Public entities still have first call on fuel supplies and since the public sector is quite extensive, this involves a substantial share at subsidized prices. Such customers still include the National Electricity and National Water Corporations, large agricultural schemes like the Gezira scheme, and the Railways Corporation, for example. Since market pricing is not officially observed, i.e. official prices are subsidized, the resultant excess demand must be channelled through an administrative allocation system. However, perhaps fortunately, once the public sector gets its share, the fuel is essentially up for bids. Even those rationed quantities of benzene and gasoil, for example, that are allocated and sold to urban consumer are often resold in black market where margins are quite high. In short, this burdensome and economically inefficient allocation and distribution system breaks down and sales respond to market price signals.

While many GOS officials do not concede the benefits of market pricing to allocate fuel, they do recognize that their attempts to control the market are largely fruitless. Thus, there is a strong movement afoot to return the decisions and logistics related to customer level fuel deliveries to the private distributing companies. Inevitably these companies will find new opportunities under such a liberalized system to respond to the market more flexibly. Moreover, the cost of administering distribution will be moved into the private sector where incentives for efficiency are much greater as is the expertise. This is in fact a significant concession, if not to the efficiency of markets, at least to the relative efficiency of the private sector over that of the public in undertaking a specific operation. Those who support it are proceeding very carefully in implementing the new system so as to disprove incipient opposition to reliance on the private sector.

IV. JUSTIFICATION FOR THE PETROLEUM COMPONENT OF THE COMMODITY IMPORT PROGRAM

A. U.S. Interests and Objectives

Basic economics -- the supply and prices of fuel, bread, sugar and other commodities -- influence Sudan's political stability and our realization of U.S. objectives throughout northeast Africa and the Middle East. Frustration with the Nimeri regime's economic policies eventually released long-developping political disillusionment with dictatorial rule. Reincarnated political activism continued to reinforce the temporary military government's commitment to democracy. Inevitably it has made Sudan's political environment increasingly sensitive to economic hardships that persist from historical mismanagement and drought.

U.S. interests in Sudan derive from its strategic location, its historically constructive approach to Middle East politics, its political and diplomatic influence in the Arab and African worlds, its recnt entry into the small club of Africa democracies, and its potential as a food exporter to the Middle East. The protection of U.S. interests in the Horn of Africa and the Nile Valley depend upon a friendly government. Certainly, constructive relations with Egypt are a prime concern. Even a simple shift in policies on control of the Nile waters could prove disastrous to the Egyptian economy. A friendly and stable government in Sudan also affects the outlook of governments in the Arabian Peninsula, and ultimately, U.S. influence in the Persian Gulf. Similarly, as our here to force largest aid program in Africa, our actions and their success attract attention and influence perceptions throughout the region. The change in government, the turnover by the military to democratic rule and its commitment to democracy have increased attention on both the Sudan and it donor.

The recent drought, which affected the entire Sahel as well as other areas in Africa, reinforced the importance of U.S. economic assistance to support strategic geopolitical interests. Drought-induced famine ignited cross border and internal population shifts that have forced people from different nationalities, tribes and economic traditions into concentrated land areas around the Blue and White Niles and along the Ethiopian and Chadian borders. The refugee population in Sudan may have exceeded one million people in 1985. Domestic population shifts, although difficult to enumerate, affected an estimated four to five million people, approximately one quarter of Sudan's population. Worsened conflicts over land rights have resulted in deaths in southern Darfur and Kordofan. Water is either unavailable in areas historically inhabited or scarce and expensive. Until the record harvest in November 1985, the price of sorghum, Sudan's staple grain, had tripled since 1983. The number who suffered severely from famine and famine-related disease has been estimated at three million people. Relief agencies operating in northern Kordofan and Darfur indicate that, even in 1986, approximately 400,000 MT of grain must be transferred to western Sudan to compensate for production shortfalls where rains ended early, leaving many crops to shrivel in the fields.

In urban areas the drought's pressures were less dramatic but politically important. Reduced exports curtailed transport services (due to lack of fuel and diversion to food relief), and overall food shortages markedly lowered urban living standards and triggered political demonstrations. Per capita GDP has declined three years in a row. With the new government in Khartoum seeking to establish a transitional phase to civilian rule, economic and political volatility has become particularly apparent.

Petroleum has historically served as a public indicator of Government performance. Petroleum shortages undoubtedly would create a degree of instability which would preclude either political or economic reform of any Government in power.

B. Developmental Impact and Rationale for Proposed Commodity

1. Continuing Objectives of Sudan's Petroleum Initiative

The provision of urgently needed petroleum supplies as a continuation of a long developping Petroleum Initiative allows us to continue our dialogue on several key issues and eventually attain important objectives. Among them are the following:

a. Consolidation and improvement of the competitive procurement system, which has renewed the willingness of major international petroleum marketing companies to submit attractive bids. The savings Sudan achieves from obtaining market fuel prices stems in part from the confidence companies have that USAID is monitoring and financing some procurements. Since the Petroleum Initiative commenced they have usually been paid in full and on time even when we were not financing the supplies.

b. To expand economic benefits by supporting the devolution of distribution responsibility to the private sector, where efficiency and flexibility is far greater. This is quite a radical move in the Sudanese context.

c. To institutionalize a mechanism, that has already commenced, for timely planning and reporting of fuel supply levels and financing needs to trigger more timely disbursements from the Central Bank of Sudan, as well as to activate increases in private fuel import licensing when scarcity dictates. More generally, we are working closely with relevant GOS officials to plan annual financing well in advance of needs and to identify likely sources early on.

d. Closely related to this, we intend to continue our dialogue on the role of pricing in efficient resource allocation, as well as in financing, through joint analysis of Sudan's present structure. This is to be a formal effort and will recommend options related to achieving supply self-sufficiency through sales revenue generation.

e. Again in a formal context, USAID and the GOS will jointly consider issues related to private fuel importation, such as how to improve the competitiveness of the import activity and what the benefits, costs, and economic impacts are of expanding such a system.

f. To further support revenue generation and supply financing efforts, USAID will continue to work with GOS to ensure that petroleum accounts are kept current. Moreover, we continue to support the use of sales revenues to help refinance a regular fuel supply.

In addition to the sector specific objectives are the broader ones of helping to maintain a stable political environment, and to facilitate a regular supply of this very critical input. Availability of fuel is, of course, a major factor in transport, electricity, and mechanized agricultural costs.

V. MARKET ANALYSIS AND CIP ALLOCATION

A. U.S. Share of Imports

In 1981/82, Sudan's imports reached a peak of $1.9 billion. Historically the U.S. has supplied only a small share of total imports--7 percent, rising to 12 percent in 1981/82 ($226 million). Western Europe and Arab countries have traditionally supplied over two-thirds of merchandise imports. The main commodities supplied by the U.S. are:

Agricultural commodities:	Wheat, wheat flour and tallow
Agricultural equipment and spare parts:	Medium and large tractors, plows, harrows, cultivators, cotton and peanut planters and harvestors, pumps and water well drilling equipment
Industrial raw materials, machinery and spare parts:	Tinplate, equipment for spinning and weaving, machinery for oil seed crushing and processing, and clay brick and cement block manufacturing
Transportation equipment and spare parts:	Primarily heavy trucks, aircraft parts, and material handling equipment
Petroleum Supplies	refined products; gasoline diesel, fuel oil

Significant market opportunities exist for telecommunications equipment, electric power generation and distribution equipment, and sugarcane harvestors and refining machinery. The key to capitalizing on these opportunities is concessional financing. Commercial sales are limited by the lack of foreign exchange and an inability to obtain supplier credits or loans from commercial sources.

The import community consists of approximately 2,000 private importers who are registered with the GOS' Ministry of Commerce, Industry and Cooperation. Public sector and parastatal enterprises are also major importers, primarily of commodities and equipment related to the construction and maintenance of infrastructural and public service facilities and the operation of the Sudan's large-scale agricultural schemes.

The official exchange rate is now $1.00 = LS 2.50. The unofficial free market rate was approximately $1.00 = LS 4.75 as of April 1986. *

B. CIP Pipeline

The following table summarizes the status of the FY 1980, FY 1981, FY 1982, FY 1983, and FY 1984 CIP programs. Also shown are projected disbursements for the proposed FY 1985 program.

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* See footnote on free foreign exchange rate, p. 51.

Table 12. CIP Pipelin(

($000)
Through FY 85

FY	Amount	Oblig	Expend	Pipeline
1980	40.0	39.9	39.9	-
1981	50.0	50.0	49.9	0.1
1982	.00.0	100.0	97.9	2.1
1983	60.2	60.2	44.4	15.8
1984	102.0	102.0	43.6	58.4
1985	111.0	110.0	-	-11.0
1986				

Source: FM/CAD Report W. 214, 9/30/85

C. Allocation of Commodities to be Procure

Financing under this CIP Grant will be restricted to $10 million in petroleum products. These supplies may be in the form of crude or refined products, such as gasoline, gasoil (diesel) or fuel oil. The exact composition will be determined during the operation of the CIP.

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VI. LOCAL CURRENCY COMPONENT

A. Counterpart Generations

As in past Commodity Import Programs, local currency proceeds generated from this Petroleum component of Sudan's Commodity Import Programs will continue to be utilized for development projects supportive of our CDSS objectives. Over the past year -- dispite the dramatic shifts within the Government of Sudan and particularly the Ministry of Finance -- USAID has initiated a considerable list of actions to improve: a) determinations of amounts of local currency generations required; b) timing of those deposits; c) tracking of the deposits and withdrawals; d) programming of the development purposes and e) monitoring project disbursements, implementation and expenditures. USAID has further refined its prioritizion of local currency uses and is finalizing the approach with the Government of Sudan.

This Petroleum component of the FY 1986 CIP represents the results of the improvements obtained thus far. It has benefitted from the finalization and negotiations with GOS on similar problems under the first tranche of the FY 1986 PL 480 Title I Program and negotiations on amendments to previous CIP's (650-K-606 and 650-K-608) to clarify GOS local currency responsibilities to assure that both the legislative and A.I.D. policy requirements are fulfilled.

Annex Q represents USAID's general description of the major problems encountered regarding local currency generations and USAID's continuing approaches to handling them.

The proposed Local Currency section for the Grant Agreement will assure better Mission and GOS programming, tracking, and project monitoring. It will reflect the findings of previous audits and a special USAID hired contractor's findings that to resolve the critical issues:

1. All agreements must make clear, and all parties to the agreements must have a clear understanding of, the timing for deposits into the Special Accounts.

2. All agreements must make clear the exchange rate to be used, and the exact method of determining the exchange rate in calculating deposits due into the Special Accounts.

3. All agreements must make clear the base to be used in determining the amount of the deposit due into the counterpart account. That is, whether it is to be based upon sales proceeds or disbursements by AID/W, arrival or usage."

B. Local Currency Stipulations

1. Amount Due. A.I.D. will require the highest legal exchange rate in effect at the time of disbursement multiplied by the amount disbursed by A.I.D. (which is reflected in the W-214 report) as the amount of Sudanese pounds to be deposited into the Special Account set up for this petroleum component of the FY 1986 CIP. As in past agreements, this will be interpreted to mean the free commercial bank rate in effect at the time of disbursement. USAID has noted that it anticipates that during the life of this program, this method of calculating amounts of local currency due the Special Account will exceed actual proceeds because of the high degree of current and anticipated subsidy.

2. Date Due. Beginning under this Agreement, GOS will be required to have deposited the required counterpart within 90 (ninety) days of the last day of the month A.I.D. made the disbursement under this Program.

C. Operational Considerations

Henceforth, to assure proper and self-sustaining tracking, USAID/Controller will rely upon the W-214 to ascertain the disbursements made by A.I.D. and thus the corresponding amount of local currency due the Special Account. The ninety days after the end of the month enables the use of the W-214 to be the basis on which the Controller determines that Local Currencies are due the Special Account and issues the Request for Collection. USAID has abandoned the use of shipping arrival dates or receipts by private companies because of the inability to track this ourselves and the reliability of the information provided us historically by GOS.

The agreement on the exchange rate and the use of the W-214 report can be problematical for a CIP because the W-214 report does not contain the exact date of disbursement. USAID's consultants and informal discussions with auditors suggested that the Mission should make arrangements to receive a report from AID/W of the detail supporting transactions contained in the W-214 that shows the date and amount of each transaction included in the W-214 report. This, of course, is an AID/W action and will take time to work out. It should be noted, however, that for the last petroleum component (FY 85), USAID did request the exact information from AID/W/M/FM and received the needed information in a timely manner. Whether this system can be formalized should be addressed in AID/W and we understand it will be the subject of an audit recommendation.

However, given the short "turn-around" time of the proposed program and the historic "stickiness" of the GOS exchange rates, USAID does not anticipate a serious problem with calculating the amount due under this proposed program. If in the unlikely event a change in the highest legal exchange rate does occur, USAID would -- again as an exception -- request the information of FM.

To assure satisfactory management and monitoring of generated local currencies, USAID has issued a Mission Order outlining procedures and responsibilities of the various USAID offices. This Mission Order is attached as Annex H. As mentioned, USAID is currently employing the services of a short term consultant who is establishing more refined defininitions of the problems faced by the USAID Mission and more refined procedures for monitoring the local currency component of this program. Once the results of the consultant's work are reviewed, estimated in April 1986, the Mission intends to refine its Mission Order.

As in the past, a portion of the FY 1986 petroleum component of the CIP local currency generations will also support Mission operations in Sudan. Within this Trust Account, funds will be utilized to meet the costs of arrival accounting being performed by a private firm under contract with USAID.

D. Trust Account Deposit

The Government of Sudan will make deposits of local currency to a Trust Account in the name of the U.S. Disbursing Officer upon request of A.I.D. and subject to approval by the GOS. Deposits into this Trust Account will be in local currency at levels proposed by USAID and agreed to by the GOS. Disbursements from the Trust Account may be made by the Government of the United States to cover the program and administrative costs of other elements of the U.S. Mission in Sudan.

VII. PROGRAM IMPLEMENTATION

A. Overview

Until late 1985, each of USAID's divisions that have implementation responsibilities did not have the depth of staff to adequately monitor the CIP. To correct this weakness, USAID had strengthened each of the offices which participate in the CIP implementation. The Supply Management Office had now staffed with a Senior Supply Management Officer and an Assistant Supply Management Officer. The Office of Project Operations, General Development Division, employed a PSC Project Officer whose duties include primarily programming and monitoring local currency generated by the program and monitoring deposits and withdrawals from the Special Account. The Controller's Office had employed a TCN Accountant, whose primary duties included monitoring the arrival accounting system, performing end-use examinations, and reviewing AID/W accounting reports. The Economic Policy and Program Officer had assigned economic analysis responsibility to a full-time US PSC economist. In addition, the petroleum component under the Energy Planning and Management Project had the task of monitoring and coordinating the technical elements of the proposed program for the GOS. The full team had thus been on board and to provide in-depth guidance and adequate monitoring of all phases of the implementation of the program.

The April 1986 evacuation of all but four USDH and one PSC has severely impacted upon USAID's ability to execute its programs. As a result, the project and program portfolio has undergone a series of emergency modifications to assure the maximum of continuity while recognizing the extreme limitations imposed. The current Petroleum CIP has been designed to meet the urgently required GOS need while reducing to the extent permitted by policy and responsible practice, USAID's management and oversight responsibilities. Two years of experience in working with the GOS General Petroleum Corporation and the Ministry of Finance on petroleum financing and planning as well as local currency issues support the contention that the approach is feasable, at least on a temporary basis.

B. Implementation Procedures

1. GOS The major GOS entities responsible for administering and implementing this CIP grant will be the Ministry of Finance and Economic Planning (MFEP), the Ministry of Energy and Mining, and the Bank of Sudan. Section V describes the operation of the Petroleum Facility and the roles of the private oil marketing companies. Further details are being decided upon between the GOS and the private oil marketing companies, USAID and other donors. A condition precedent to disbursement of any funds under this grant requires USAID approval of these arrangements.

The Ministry of Finance and Economic Planning has been responsible for the management of the Special Account for counterpart generations. While staff at the Ministry has been able to adequately carry on this function to date, the amount of work will grow as overall levels of counterpart generations increase by $170 million a year, including both PL 480 Title I and III as well as CIP local currencies. Consequently, as ability to manage these funds becomes more difficult, improved staffing to oversee this function is being required by another CIP agreement.

2. A.I.D. The USAID Project Manager for the Petroleum CIP will be the Senior Commodity Management Officer. He will be responsible for monitoring: (i) GOS operation of the Petroleum Facility; (ii) relations between the Government and the private oil companies; (iii) GOS performance in living up to the conditions and covenants in the Program Agreement; (iv) coordination with other donors contributing to the Facility; and (v) all other operational matters related to the successful achievement of the objectives of the program. In addition, the Senior CMO, in cooperation with support officers in AID/Washington, will have responsibility for monitoring and expediting procurement of petroleum supplies. The USAID/Sudan Controller will be responsible for monitoring the generation of counterpart funds due the Special Account, performing reviews of arrival accounting and carrying out end-use monitoring to ascertain the effective arrival and utilization of CIP-financed commodities. The USAID General Development Officer will be responsible for programming counterpart funds generated by this CIP.

C. Procurement Financing Procedures and Financial Analysis

Procurement and financing procedures under this CIP will follow those set forth in AID Regulation 1. Under the conditions of this Program, all procurement will follow the procedures previously approved, which faster competition. These procedures are considered negotiated procedures under Regulation 1. The method of financing normally will be through bank Letters of Credit.

USAID will issue a Letter of Commitment in an amount of $10 million to a U.S. bank selected by the GOS. The supplier's certificate and agreement with AID (Form AID 282) will be used.

The new L/COM will require full compliance with the provisions of AID Regulation 1, as amended.

D. Eligible Commodities

Petroleum crude and refined products will be the only eligible commodities under this Program.

E. Procurement Restrictions/Limitations

This grant will be restricted to Code 935 sources and origins for commodities and related incidental services. Annex D provides a detailed justification for a source/origin waiver.

Local agents are not required by Sudanese regulations. Thus, there is no conflict with the AID Regulation 1 requirement that U.S. suppliers may sell directly to importers. All provisions of AID Regulation 1 regarding commodity eligibility review, price eligibility, and both prior review and post audit will apply to all transactions.

The Cargo Preference Act establishes requirements for the use of U.S-flag vessels whwn ocean transportation service may be used to transport U.S Government-financed commodities. In summary, the Act requires that at least 50 percent of the gross tonnage of all A.I.D-financed commodities which may be transported on ocean vessels (computed separately for dry bulk carriers, dry cargo liners and tankers) shall be transported on privately owned U.s-flag commercial vessels, to the extent such vessels are available at fair and reasonable rates. At least 50 percent for the gross freight revenue generated by all shipments of A.I.D-financed commodities transported to the cooperating country on dry cargo liners shall be paid to or for the benefit of privately owned U.S-flag vessels, to the extent such vessels are available. When shipping is chartered for a quantatitive unit of cargo, U.S-flag vessels are to be used for a least 50 percent of the quantatitive unit, if U.S-flag vessels are available at fair and reaseonable rates, before any movement is made of a non U.S-flag vessels.

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F. <u>Commodity Eligibility Date</u>

The Eligibility Date for Commodities and Commodity Related Services procured under this FY 1986 CIP will be the date of the signing of the Agreement.

G. <u>Terminal Disbursement Date</u>

The grant's Terminal Disbursement Date (TDD) will be 42 months from the date conditions precedent are met.

H. <u>Port Clearance and Inland Transportation</u>

Sudan has one major seaport--Port Sudan. It comprises 15 berths, of which two can be used for tanker off-loading of crude oil and refined products. Operational efficiency is reasonable. From the port, there is a crude pipeline able to transport over 30,000 bpd to the Port Sudan Refinery. There is now plenty of excess capacity in this pipeline. There is also piping to nearby refined products storage tanks owned by the four marketing companies. Currently there is 109,000 MT of crude storage at the refinery and 99,000 MT of storage for refined products near the port. Two Romanian-financed storage tanks were added to the port in 1985. Present port facilities allow off-loading of petroleum supplies at a rate of 200 MT/per hour although tankers can discharge 1000 MT/per hour. The GPC plans to upgrade the port facilities to 1000 mt per hour. There appears to be more than adequate capacity at Port Sudan to efficiently handle increases in petroleum supplies, although there must be careful scheduling of shipments between the GPC and the port authorities.

Inland transport of petroleum products is arranged by road, rail, pipeline and, to a limited extent, river transport. For most products there is no problem with transportation capacity. Fuel oil, however, presents a problem in that its viscosity requires it to be moved in rail-tanker cars, of which there is a shortage. Scheduling problems interfere with the use of available cars. The GOS has plans however to dedicate special block trains to moving fuel oil.

A.I.D. will apply the standard 90 days port clearance and the 12 months utilization period requirements. These, with constant follow-up and pressure on both buyers and transportation officials, should serve to expedite the movement of A.I.D.-financed supplies. At present, there is a much reduced backlog of GOS public sector imports awaiting inland transportation in holding areas outside the port.

I. <u>Methods of Implementation and Financing</u>

Method of Implementation	Method of Financing	Approximate Amount
Petroleum, Host Country Procurement	Bank L/COM	$10.0 million

The GPC has an arrival and supply clearance unit established at Port Sudan for petroleum imports. This office serves as a "Customs Broker" and forwarding agent.

For Commodity Import Programs in general, the Mission has determined that records maintained by the GOS are not adequate for our purposes. Therefore, USAID has established a system that adequately tracks commodity arrival and movement through the port, indicating shortages, breakage and distribution to the ultimate end-user. Up to this point in time, USAID has records on approximately 21 percent of all CIP transactions from the FY 1981 through FY 1984 programs. This will be expanded and will include most of the high cost items under those programs. The Mission randomly selects the transactions to be accounted for. USAID's contractor performs the detailed work and prepares reports that indicate arrivals compared to shipments and reflects overages, shortages, and breakage. These reports are transmitted to the Supply Management Office for any necessary action. The contract is funded from local currency generated under the program. However, for the petroleum section of the CIP, all petroleum imports are recorded.

In fiscal year 1983, USAID/Sudan initiated a program of end-use examinations of both private and public sector end-users. A report of findings is prepared for each examination. The report is forwarded to Mission senior management for information and to the Supply Management Office for any action that might be indicated by negative findings.

The Regional Inspector General in Nairobi is currently planning to include an audit of the Commodity Import Program in his FY 1985 audit schedule. This audit in conjunction with the FY 1984 CIP evaluation, existing arrival accounting system, and program of end-use examinations will provide necessary assurances that procured commodities are effectively used. At the same time, the GOS will covenant that it will contract with an internationally respected accounting firm to periodically audit the Petroleum Facility (see Section V for details).

J. Import Controls

Under the existing system, the GPC establishes levels and timing of petroleum shipments based on historical needs and an estimation of future consumption. The GPC then alerts the Ministry of Finance and Economic Planning of planned import levels which are then adjusted in light of the expected availability of foreign exchange. The Ministry of Finance and Economic Planning requests the Bank of Sudan to set aside sufficient foreign exchange. The Ministry of Commerce, Industry and Cooperation issues petroleum import licences automatically to the GPC following their application, as petroleum is considered an essential public import. Petroleum comprises a major portion of the foreign exchange budget for official imports.

K. Control of CIP Funds

Actual disbursement of any funds by USAID will be dependent upon the supplier providing a full set of payment documentation, including Form II (Commodity and Price Eligibility Approval), the USAID Supplier's Certificate attesting to compliance with a number of USAID regulatory concerns, and evidence that the cargo has actually been shipped. Concurrent follow-up by both USAID and the importer concerning arrivals will match received goods with paid shipments. This will assure that CIP-financed commodities are received and, ultimately through end-use checks, that the commodities are used as intended for the benefit of the Sudan's economy.

L. Evaluation of Performance and Economic Impact

Monitoring and evaluating GOS' performance during the implementation of the Petroleum Facility CIP and the economic impact of the program are important considerations. By the GOS contracting with an internationally respected accounting firm to monitor the financial aspects of the program, one element is covered. Monitoring and evaluating other elements of the program (for example the allocation system) will be undertaken jointly by USAID and the GOS, with technical services under the Energy Planning and Management Project (see Section VIII M below). Monitoring and evaluating performance and economic impact will be undertaken on a timely basis to coincide with USAID decisions regarding incremental obligations scheduled for FY 1987 and 1988, so that our decisions will be based on solid evidence and hard data.

M. Related Technical Services

The grant assistance proposed for the Petroleum Facility will be used entirely for the purpose of procuring petroleum products. If technical services or technical assistance is required by the Ministry of Energy and Mining, the General Petroleum Corporation or the Petroleum Facility group, approved services can be provided under the DA-financed Energy Planning and Management Project (650-0059). Under this project, a contract has been executed with Energy/Development International for short- and long-term technical assistance. The development of the Petroleum Facility is a result of work initiated by Energy/Development International under a previous contract in 1982/83.

VIII. OTHER CONSIDERATIONS

A. Impact on U.S. Balance of Payments

The Petroleum Initiative CIP Program will have no impact on U.S. exports and balance of payments, since the U.S. is a net importer of oil. U.S. exports to Sudan amounted to $22.6 million in 1981/82, which was only about 0.1 percent of total U.S. exports. The U.S. share of Sudan's imports amounted to $12.5 million in 1981/82, or 3.3 percent of total Sudanese imports.

B. Internal Financial Effects

The generation and expenditure of local currency under the CIP program are probably somewhat deflationary in that the sale of imported commodities absorbs excess liquidity, and expenditures of local currency lag behind generations from sales. To the extent that CIP commodities are sold to the private sector with local currency accruing to the GOS, resources are diverted from the private to the public sector.

C. Use of U.S. Government Excess Property

Given the nature of the items for which this CIP will be utilized, U.S. Government excess property is not relevant.

D. Relation to Export-Import (Ex-Im) Bank Credits

The Ex-Im Bank currently has an exposure in Sudan of about $20 million. This total includes $16 million in project loans and $4 million in guarantees and insurance. Past deliquencies of $2.7 million, which caused the suspension of further U.S. supplier credits to Sudan, were rescheduled early in 1980. Ex-Im activity toward increased exposure is to be determined subsequent to a review of the Sudanese ability to meet the rescheduled debt commitments.

Two small Foreign Credit Insurance Association (FCIA) loans were completed in 1980, based upon long standing past acceptances. However, nothing new has been considered. The CIP grant for FY 1985 will complement, not conflict, with the Ex-Im Bank activities.

E. Relation to the Overseas Private Investment Corporation (OPIC) Program

OPIC was established to promote U.S. private investment in developing countries by making loans to overseas ventures and providing insurance against war, currency inconvertability and expropriation. For Sudan, OPIC emphasizes transportation and agricultural projects.

As of March 31, 1984, OPIC had 15 active contracts with six companies with insurance coverage ranging from $415,000 to $125 million. Applications to cover $30 million of investment were pending.

This CIP is not expected to directly assist firms which have an existing contract or pending application but complements OPIC support of the private sector.

IX. RECOMMENDATIONS, TERMS AND CONDITIONS

A. Recommendations

Based on the USAID determination that this CIP[is an integral part of GOS and the international donor community's objectives for Sudan's stabilization and recovery, it is recommended that a grant of ten million dollars ($10,000,000) in FY 1986 to the Government of the Republic of Sudan be authroized for the financing and importing of petroleum products. It is further recommended that a waiver of source/origin from Code 941 to Code 899 be approved.

B. Terms and Conditions

1. Conditions Precedent

a) An opinion of the Attorney General, or his designee, of the Democratic Republic of the Sudan that this Agreement has been duly authorized and/or ratified by, and executed on behalf of, the Grantee, and that it constitutes a valid and legally binding obligation of the Grantee in accordance with all of its terms.

b) A statement representing and warranting that the named person or persons have the authority to act as the representative or representatives of the Grantee, together with a specific signature of each person certified as to its authenticity.

2. Notification When A.I.D. has determined that the conditions precedent specified above have been met, it will promptly notify the Grantee.

3. Terminal Date for Conditions Precedent If all the conditions precedent specified above have not been met within one hundred and twenty (120) days from the date of this Agreement, or such later date as A.I.D. may specify in writing, A.I.D., at its option, may terminate this Agreement by written notice to Grantee.

Annex A

Initial Environmental Examination or Categorical Exclusion

Project Country: Sudan

Project Title: Petroleum Initiative Commodity Import Program Grant

Funding: ESF FY (s) 1986 $ 10,000,000

IEE prepared by: John Gaudet, Regional Environment Officer

Environmental Action Recommended:

Positive Determination________
Negative Determination XXX

Categorical Exclusion:

This activity meets the criteria for Categorical Exclusion in accordance with Section 216.2 (C) and is excluded from further review because:

Concurrence: Approved: Wes Fisher

Bureau Environmental Officer Disapproved: May 27, 1986

Date: ________

Clearance: CG/AFR Date 5/30/86

Examination of Nature, Scope and Magnitude of Environmental Impacts:

I. Description of the Project.

The project proposes to provide a Commodity Import Grant of $10 million to the Government of Sudan (GOS) from the Economic Support Fund on standard A.I.D. terms. The principal objective of this grant is to help assure a sufficient and reliable supply of petroleum (and to encourage Sudan's progress in the establishment of an efficient system for the financing, procuring, importing, allocating and distributing of petroleum products for the Sudanese economy.)

Commodities will be limited to petroleum products. However, it is not possible at this time to determine the amounts which might be in the form of crude or refined products (e.g. fuel oil, gasoline or gasoil). Each of these forms of petroleum has greatly different uses. Furthermore, USAID's contribution will be part of a larger petroleum initiative in which our contribution is approximately only 11 percent. At the same time, we will have no control over its use as this will be determined by the GOS and the four private oil marketing companies.

Although the general category of commodity has been identified as "petroleum, crude or refined", and because USAID cannot exert control over its use, it would be impossible at this time to define the magnitude of environmental impacts expected. In general, however, these impacts are not significant when compared to the enormous environmental problems now resulting from the improper management of renewable energy resources. Consequently, USAID/Sudan has initiated several activities in the area of renewable energy and natural resource sectors to help the host country cope with environmental problems relative to proper management and conservation of energy.

2. Recommended Environmental Action.

The GOS is well aware of USAID's concern regarding environmental effects of misuse of energy resources, but these concerns will be again brought to their attention prior to signing the grant agreement.

On the basis of the above information, a negative determination is requested. Mission appreciates early response.

Action requested by:______________________________
John W. Koehring, Mission Director

Concurrence: Approved:

Bureau Environmental Officer Disapproved:

Date:

Clearance: CG/AFR__________Date_____

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Annex B

3A(2) - NONPROJECT ASSISTANCE CHECKLIST

The criteria listed in Part A are applicable generally to FAA funds, and should be used irrespective of the program's funding source. In part B a distinction is made between the criteria applicable to Economic Support Fund Assistance and the criteria applicable to Development Assistance. Selection of the criteria will depend on the funding source for the program.

CROSS-REFERENCES: IS COUNTRY CHECKLIST UP TO DATE? IDENTIFY. HAS STANDARD ITEM CHECKLIST BEEN REVIEWED?

A. GENERAL CRITERIA FOR NONPROJECT ASSISTANCE

1. FY 1986 Continuing Resolution Sec. 524; FAA Sec. 634A.

   Describe how authorizing and appropriations committees of Senate and House have been or will be notified concerning the project.

   No congressional Notification required because notice contained in Congressional Presentation.

2. FAA Sec. 611(a)(2). If further legislative action is required within recipient country, what is basis for reasonable expectation that such action will be completed in time to permit orderly accomplishment of purpose of the assistance?

   None required

3. FAA Sec. 209. Is assistance more efficiently and effectively given through regional or multilateral organizations? If

   No
   N/A

so why is assistance not so given? Information and conclusion whether assistance will encourage regional development programs.

4. FAA Sec. 601(a). Information and conclusions whether assistance will encourage efforts of the country to: (a) increase the flow of international trade: (b) foster private initiative and competition; (c) encourage development and use of cooperatives, credit unions, and savings and loan associations; (d) discourage monopolistic practices; (e) improve technical efficiency of industry, agriculture, and commerce; and (f) strengthen free labor unions.

a) Assistance provides essential petroleum imports used for export production.
b) Assistance will support competive private sector petroleum marketing.
c) N/A.
d) Program encourages competition in petroleum purchasing.
e) Increased petroleum imports allow fuller utilization of industrial and agricultural capacity.
f) N/A.

5. FAA Sec. 601(b) Information and conclusions on how assistance will encourage U.S. private trade and investment abroad and encourage private U.S. participation in foreign assistance programs (including use of private trade channels and the services of U.S. private enterprise).

Program encourages greater private sector participation in petroleum purchases through a "guarantee" system. Significant Participation is anticipated for a U.S. private oil company.

6. FAA Sec. 612(b); Sec. 636(h); FY 1986 Continuing Resolutation Sec. 507. Describe steps taken to assure that, to the maximum extent possible, the country is contributing local currencies to meet the cost of contractual and other services, and foreign currencies owned by the U.S. are utilized in lieu of dollars.

Recent CIP evaluation, Quarterly Reviews of GOS/USG funded local currency projects recent audits confirm proper contributions, uses, drawdowns and reporting on CIP generated local currencies.

7. FAA Sec. 612(d). Does the U.S. own excess foreign currency of the country and, if so, what arrangements have been made for its release?

   No

8. FAA Sec. 601(e). Will the assistance utilize competitive selection procedures for the awarding of contracts, except where applicable procurement rules allow otherwise?

   Yes

9. FAA 121(d). If assistance is being furnished under the Sahel Development Program, has a determination been made that the host government has an adequate system for accounting for and controlling receipt and expenditure of A.I.D. funds?

   N/A

10. FY 1986 Continuing Resolution Sec. 533. Is disbursement of the assistance conditioned solely on the basis of the policies of any multilateral institution?

    No

B. FUNDING CRITERIA FOR NON PROJECT ASSISTANCE

1. Nonproject Criteria for Economic Support Fund

   a. FAA Sec. 531(a). Will this assistance promote economic and political stability? To the maximum extent feasible, is this assistance consistent with the policy directions, purposes, and programs of part I of the FAA?

   Yes. As one of Sudan's three essential imports, petroleum is a critical input to both irrigated and rainfed agriculture. Shortages cause economic descriptions and political unrest. Greater and more regular supplies promote economic and political stability. See full explanation Section III.

   b. FAA Sec. 531(c). Will assistance under this chapter be used for military, or paramilitary activities?

   No

c. <u>FAA Sec. 531(d)</u>. Will ESF funds made available for commodity import programs or other program assistance be used to generate local currencies? If so, will such local currencies be available to support activities consistent with the objectives of FAA sections 103 through 106?	Yes. Local Currencies are carefully programmed and monitored to conform with Sections 103 through 106 of the FAA as well as the specific development objectives of GOS and USAID. Annex C details in full support for this response.
d. <u>ISDCA of 1985 Sec. 205</u>. Will ESF funds made available for commodity import programs be used for the purchase of agricultural commodities of United States-origin? If so, what percentage of the funds will be so used?	N/A. Second section of CIP will address this criterion.
e. <u>ISDCA of 1985 Sec. 801</u>. If ESF funds will be used to finance imports by an African country (under a commodity import program or sector program), will the agreement require that those imports be used to meet long-term development needs in those countries in accordance with the following criteria?	
(i) spare parts and other imports shall be allocated on the basis of evaluations, by A.I.D., of the ability of likely recipients to use such spare parts and imports in a maximally productive, employment generating, and cost effective way;	Yes. This CIP and USAID analyses have been developed in conjunction with similar analyses done by IMF and World Bank which confirm the productive, employment generating and cost-effective advantages (of the proposed approach.) This
(ii) imports shall be coordinated with investments in accordance with the recipient country's plans for promoting economic development. A.I.D. shall	Yes. CIP is integral part of GOS Essential Import and Three Year Investment Plan.

assess such plans to determine whether they will effectively promote economic development;

(iii) emphasis shall be place on imports for agricultural activities which will expand agricultural production, particularly activities which expand production for export of production to reduce reliance on imported agricultural products;

(iv) emphasis shall also be place on a distribution of imports having a broad development impact in terms of economic sectors and geographic regions;

Agriculture, the direct beneficiary of CIP, supports 80% of Sudan's population.

(v) in order to maximize the likelihood that the imports financed by the United States under the ESF Chapter are in addition to imports which would otherwise occur, consideration shall be given to historical patterns of foreign exchange uses;

CIP maintains historic patterns of foreign exchange uses for essential imports, but now allows possibility for US supplier and/or local subsidiary to participate.

(vi)(A) seventy-five percent of the foreign currencies generated by the sale of such imports by the government of the country shall be deposited in a special account established by that government and, except as provided in subparagraph (B), shall be available only for use in accordance with the agreement for economic development activities

Yes. See Annex C.

which are consistent with the policy directions of section 102 of the FAA and which are the types of activities for which assistance may be provided under sections 103 through 106 of the FAA;

(B) the agreement shall require that the government of the country make available to the United States Government such portion of the amount deposited in the special account as may be determined by the President to be necessary for requirements of the United States Government.

Agreement will, as in the past, include this requirement.

f. ISDCA of 1985 Sec. 207. Will ESF funds be used to finance the construction of, or the operation or maintenance of, or the supplying of fuel for, a nuclear facility? If so, has the President certified that such country is a party to the Treaty on the Non-Proliferation of Nuclear Weapons or the Treaty for the Prohibition of Nuclear Weapons in Latin American (the "Treaty of Tlatelolco"), cooperates fully with the IAEA, and pursues nonproliferation policies consistent with those of the United States?

No.

g. FAA Sec. 609. If commodities are to be granted so that sale proceeds will accrue to the recipient country, have Special Account (counterpart) arrangements been made?

Yes.

2. Nonproject Criteria for Development Assistance

a. FAA Sec. 102(a); Sec. 111; 113, 281(a). Extent to which activity will (a) effectively involve the poor in development, by extending access to economy at local level; increasing labor-intensive production and the use of appropriate technology, spreading investment out from cities to small towns and rural areas, and insuring wide participation of the poor in the benefits of development on a sustained basis, using the appropriate U.S. institutions; (b) help develop cooperatives, especially by technical assistance, to assist rural and urban poor to help themselves toward better life, otherwise encourage democratic private and local governmental institutions; (c) support the self-help efforts of developing countries; (d) promote the participation of women in the national economic of developing countries and the improvement of women's status; and (e) utilize and encourage regional cooperation by developing countries?

N/A

b. FAA Sec. 103, 103A, 104, 105, 106, 107. Is assistance being made available: (include only applicable paragraph which corresponds to source of funds used. If more than one fund source is used for assistance, include relevant paragraph for each fund source.)

N/A

(1) [103] for agriculture, rural development or nutrition; if so, (a) extent to which activity is specifically designed to increase productivity and income of rural poor; [103] if for agricultural research, full account shall be taken of the needs of small farmers; and extensive use of field testing to adapt basic research to local conditions shall be made; (b) extent to which assistance is used in coordination with efforts carried out under Sec. 104 to help improve nutrition of the people of developing countries through encouragement of increased production of crops with greater nutritional value, improvement of planning, research, and education with respect to nutrition, particularly with reference to improvement and expanded use of indigenously produced foodstuffs; and the undertaking of pilot or demonstration of poor and vulnerable people; and (c) extent to which activity increases national food security by improving food policies and management and by strengthening national food reserves, with particular concern for the needs of the poor, through measures encouraging domestic production, building national food reserves, expanding available storage facilities, reducing post harvest food losses, and improving food distribution.

N/A

collection and analysis, the training of skilled personnel, research on and development of suitable energy sources, and pilot projects to test new methods of energy production; and (b) facilitative of geological and geophysical survey work to locate potential oil, natural gas, and coal reserves and to encourage exploration for potential oil, natural gas, and coal reserves.

(ii) technical cooperation and evelopment activities, especially with U.S. private and voluntary, or regional and international development, organizations; N/A

(iii) research into, and evaluation of, economic development processes and techniques; N/A

(iv) reconstruction after natural or manmade disaster; N/A

(v) for special development problems, and to enable proper utilization of earlier U.S. infrastructure, etc., assistance; N/A

(vi) for special development, especially small labor-intensive enterprises, marketing systems, and financial or other institutions to help urban poor participate in economic and social development. N/A

(2) [104] for population planning under Sec. 104(b) or health under Sec. 104(c); if so, extent to which activity emphasizes low-cost, integrated delivery systems for health, nutrition and family planning for the poorest people, with particular attention to the needs of mothers and young children, using paramedical and auxiliary medical personnel, clinics and health posts, commercial distribution systems and other modes of community research.

N/A

(3) [105] for education, public administration, or human resources development; if so, (a) extent to which activity strengthens nonformal education, makes formal education more relevant, especially for rural families and urban poor, or strengthens management capability of institutions enabling the poor to participate in development; and (b) extent to which assistance provides advanced education and training of people in developing countries in such disciplines as are required for planning and implementation of public and private development activities.

N/A

(4) [106] for technical assistance, energy, research, reconstruction, and selected development problems; if so, extent activity is: (i)(a) concerned with data

N/A

(5) [107] is appropriate effort placed on use of appropriate technology? (Relatively smaller, cost-saving, labor using technologies that are generally most appropriate for the small farms, small businesses, and small incomes of the poor.)

N/A

c. FAA 118(c) and (d). Does the assistance comply with the environmental procedures set forth in AID Regulation 16. Does the assistance take into consideration the problem of the destruction of tropical forests?

N/A

d. FAA Sec. 281(b) Describe extent to which the activity recognizes the particular needs, desires, and capacities of the people of the country; utilizes the country's intellectual resources to encourage institutional development; and supports civic education and training in skills required for effective participation in governmental and political processes essential to self-government.

N/A

e. FAA Sec. 122(b) Does the activity give reasonable promise of contributing to the development of economic resources, or to the increase of productive capacities and self-sustaining economic growth?

Yes.

3A(3) - STANDARD ITEM CHECKLIST

Listed below are the statutory items which normally will be covered routinely in those provisions of an assistance agreement dealing with its implementation, or covered in the agreement by imposing limits on certain uses of funds.

These items are arranged under the general headings of (A) Procurement, (B) Construction, and (C) Other Restrictions.

A. PROCUREMENT

1. FAA Sec. 602. Are there arrangements to permit U.S. small business to participate equitably in the furnishing of commodities and services financed?	N/A
2. FAA Sec. 604(a). Will all procurement be from the U.S. except as otherwise determined by the President or under delegation from him?	Yes. A waiver of source-origin is being requested.
3. FAA Sec. 604(d). If the cooperating country discriminates against marine insurance companies authorized to do business in the U.S., will commodities be insured in the United States against marine risk with such a company?	N/A
4. FAA Sec. 604(e); ISDCA of 1980 Sec. 705(a). If offshore procurement of agricultural commodity or product is to be financed, is there provision against such procurement when the domestic price of such commodity is less than parity? (Exception where commodity financed could not reasonably be procured in U.S.)	N/A

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5. FAA Sec. 604(g). Will construction or engineering services be procured from firms of countries which receive direct economic assistance under the FAA and which are otherwise eligible under Code 941, but which have attained a competitive capability in international markets in one of these areas? Do these countries permit United States firms to compete for construction or engineering services financed from assistance programs of these countries? N/A

6. FAA Sec. 603. Is the shipping excluded from compliance with requirement in section 901(b) of the Merchant Marine Act of 1936, as amended, that at least 50 per centum of the gross tonnage of commodities (computed separately for dry bulk carriers, dry cargo liners, and tankers) financed shall be transported on privately owned U.S. flag commercial vessels to the extent such vessels are available at fair and reasonable rates?

7. FAA Sec. 621. If technical assistance is financed, will such assistance be furnished by private enterprise on a contract basis to the fullest extent practicable? If the facilities of other Federal agencies will be utilized, are they particularly suitable, not competitive with private enterprise, and made available without undue interference with domestic programs? Yes.

8. International Air Transportation Fair Competitive Practices Act, 1974. If air transportation of persons or property is financed on grant basis, will U.S. carriers be used to the extent such service is available? N/A

9. FY 1986 Continuing Resolution Sec. 504. If the U.S. Government is a party to a contract for procurement, does the contract contain a provision authorizing termination of such contract for the convenience of the United States? N/A

B. Construction

1. FAA Sec. 601(d). If capital (e.g., construction) project, will U.S. engineering and professional services be used? N/A

2. FAA Sec. 611(c). If contracts for construction are to be financed, will they be let on a competitive basis to maximum extent practicable? N/A

3. FAA Sec. 620(k). If for construction of productive enterprise, will aggregate value of assistance to be furnished by the U.S. not exceed $100 million (except for productive enterprises in Egypt that were described in the CP)? N/A

C. Other Restrictions

1. FAA Sec. 122(b). If development loan, is interest rate at least 2% per annum during grace period and at least 3% per annum thereafter?

N/A

2. FAA Sec. 301(d). If fund is established solely by U.S. contributions and administered by an international organization, does Comptroller General have audit rights?

N/A

3. FAA Sec. 620(h). Do arrangements exist to insure that United States foreign aid is not used in a manner which, contrary to the best interests of the United States, promotes or assists the foreign aid projects or activities of the Communist-bloc countries?

Yes.

4. Will arrangements preclude use of financing:

a. FAA Sec. 104(f); FY 1986 Continuing Resolution Sec. 526. (1) To pay for performance of abortions as a method of family planning or to motivate or coerce persons to practice abortions; (2) to pay for performance of involuntary sterlization as method of family planning, or to coerce or provide financial incentive to any person to undergo

Yes.

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sterilization; (3) to pay for any biomedical research which relates, in whole or part, to methods or the performance of abortions or involuntary sterilizations as a means of family planning; (4) to lobby for abortion?

b.	FAA Sec. 488. To reimburse persons, in the form of cash payments, which illicit drug crops are eradicated?	Yes
c.	FAA Sec. 620(g). To compensate owners for expropriated nationalized property?	Yes.
d.	FAA Sec. 660. To provide training or advice or provide any financial support for police, prisons, or other law enforcement forces, except for narcotics programs?	Yes.
e.	FAA Sec. 636(i). For purchase, sale, long-term lease, exchange of guaranty of the sale of motor vehicles manufactured outside U.S., unless a waiver is obtained?	Yes.

g. FY 1986 Continuing Resolution, Sec. 503. To pay pensions, annuities, retirement pay, or adjusted service compensation for military personnel? — Yes.

h. FY 1986 Continuing Resolution, Sec. 505. To pay U.N. assessments, arrearages or dues? — Yes.

i. FY 1986 Contining Resolution, Sec. 506. To carry out provisions of FAA section 209(d) (Transfer of FAA funds to multilateral organizations for lending)? — Yes.

j. FY 1986 Continuing Resolution, Sec. 510. To finance the export of nuclear equipment, fuel, or technology? — Yes.

k. FY 1986 Continuing Resolution, Sec. 511. For the purpose of aiding the efforts of the government of such country to repress the legitimate rights of the population of such country contrary to the Universal Declaration of Human Rights? — Yes.

l. FY 1986 Continuing Resolution, Sec. 516. To be used for publicity or propaganda purpose within U.S. not authorized by Congress? — Yes.

5c(1) - COUNTRY CHECKLIST

Listed below are statutory criteria applicable generally to FAA funds, and criteria applicable to individual fund sources: Development Assistance and Economic Support Fund.

A. GENERAL CRITERIA FOR COUNTRY ELIGIBILITY

1. FAA Sec. 481(h)(1); FY 1986 Continuing Resolution Sec. 527. Has it been determined or certified to the Congress by the President that the government of the recipient country has failed to take adequate measures or steps to prevent narcotic and psychotropic drugs or other controlled substances (as listed in the schedules in section 202 of the Comprehensive Drug Abuse and Prevention Control Act of 1971) which are cultivated, produced or processed illicitly, in whole or in part, in such country or transported through such country, from being sold illegally within the jurisdiction of such country to United States Government personnel or their dependents or from entering the United States unlawfully?

   No.

2. FAA Sec. 481(h)(4). Has the President determined that the recipient country has not taken adequate steps to prevent (a) the processing, in whole or in part, in such country of narcotic and psychotropic durgs or other controlled substances, (b) the transportation through such country of narcotic and psychotropic drugs or other controlled substances, and (c) the use of such country as a refuge of illegal drug traffickers?

   No.

3. FAA Sec. 620(c). If assistance is to a government, is the government liable as debtor or unconditional guarantor on any debt to a U.S. citizen for goods or services furnished or ordered where (a) such citizen has exhausted available legal remedies and (b) the debt is not denied or contested by such government? — No

4. FAA Sec. 620(e)(1). If assistance is to a government, has it (including government agencies or subdivisions) taken any action which has the effect of nationalizing, expropriating, or otherwise seizing ownership or control of property of U.S. citizens or entities beneficially owned by them without taking steps to discharge its obligations toward such citizens or entities? — No

5. FAA Sec. 620(a), 620(f), 620D; FY 1986 Continuing Resolution Sec. 512. Is recipient country a Communist country? If so, has the President determined that assistance to the country is important to the national interests of the United States? Will assistance be provided to Angola, Cambodia, Cuba, Iraq, Syria, Vietnam, Libya, or South Yemen? Will assistance be provided to Afghanistan without a certification? — No

6. FAA Sec. 620(j). Has the country permitted, or failed to take adequate measures to prevent, the damage or destruction by mob action of U.S. property? — No

7. FAA Sec. 620(l). Has the country failed to enter into an agreement with OPIC?

No.

8. FAA Sec. 620(o); Fishermen's Protective Act of 1967, as amended, Sec. 5. (a) Has the country seized, or imposed any penalty or sanction against, any U.S. fishing activities in international waters?

No

(b) If so, has any deduction required by the Fishermen's Protective Act been made?

No.

9. FAA Sec. 620(q); FY 1986 Continuing Resolution Sec. 518. (a) Has the government of the recipient country been in default for more than six months on interest or principal of any AID loan to the country?

At present, Sudan is not in arrears on loan payments to AID.

(b) Has the country been in default for more than one year on interest or principal on any U.S. loan under a program for which the appropriation bill (or continuing resolution) appropriates funds?

No. While it currently appears that Sudan may be more than one year in arrears on June 7, 1986, obligation will not be incurred on or after that date.

10. FAA Sec. 620(s). If contemplated assistance is development loan or from Economic Support Fund, has the Administrator taken into account the amount of foreign exchange or other resources which the country has spent on military equipment? (Reference may be made to the annual "Taking into Consideration" memo: "Yes, taken into account by the Administrator at time of approval of Agency OYB." This approval by the Administrator of the Operational Year Budget can be the basis for an affirmative answer during the fiscal year unless significant changes in circumstances occur.)

Yes. Taken into account by the Administrator at time of approval of Agency OYB.

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11. FAA Sec. 620(t). Has the country servered diplomatic relations with the United States? If so, have they been resumed and have new bilateral assistance agreements been negotiated and entered into since such resumption?

No.

12. FAA Sec. 620(u). What is the payment status of the country's U.N. obligations? If the country is in arrears were such arrearages taken into account by the AID Administrator in determining the current AID Operational Year Budget? (Reference may be made to the Taking into Consideration memo.)

Sudan was not considered to be in arrears as of this writing.

13. FAA Sec. 620A; Has the government of the recipient country aided or abetted, by granting sanctuary from prosecution to, any individual or group which has committed an act of international terrorism?

No.

14. ISDCA of 1985 Sec. 552(b). Has the Secretary of State determined that the country is a high terrorist threat country after the Secretary of Transportation has determined, pursuant to Section 1115(e)(2) of the Federal Aviation Act of 1958, that an airport in the country does not maintain and administer effective security measures?

No.

15. FAA Sec. 666. Does the country object, on the basis of race, religion, national origin or sex, to the presence of any officer or employee of the U.S. who is present in such country to carry out economic development programs under the FAA. — No.

16. FAA Sec. 669, 670. Has the country after August 3, 1977, delivered or received nuclear enrichment or reprocessing equipment, materials, or technology, without specified arrangements or safeguards? Has it transferred a nuclear explosive device to a non-nuclear weapon state, or if such a state, either received or detonated a nuclear explosive device? (FAA Sec. 602E permits a special waiver of Sec. 669 for Pakistan.) — No

17. FAA Sec. 670. If the country is a non-nuclear weapon state, has it, on or after August 8, 1985, exported illegally (of attempted to export illegally) from the United States any material, equipment, or technology which would contribute significantly to the ability of such country to manufacture a nuclear explosive device? — No

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18. ISDCA of 1981 Sec. 720. Was the country represented at the Meeting of Ministers of Foreign Affairs and Heads of Delegation of the Non-Aligned Countries to the 36th General Assembly of the U.N. of Sept. 25 and 28, 1981, and failed to disassociate itself from the communique issued? If so, has the President taken it into account? (Reference may be made to the Taking into Consideration memo).

Sudan was represented at this meeting and to date has not disassociated itself with the communique in question. This action on the part of Sudan has been considered by the U.S. Government (see Taking into account memo dated January 15, 1982) in approving the Agency's FY 86 OYB.

19. FY 1986 Continuing Resolution Sec. 541.

Are any of the funds to be used for the performance of abortions as a method of family planning or to motivate or coerce any person to practice abortions?

No.

Are any of the funds to be used to pay for the performance of involuntary sterilization as a method of family planning or to coerce or provide any financial incentive to any person to undergo sterilizations?

No.

Are any of the funds to be used to pay for any biomedical research which relates, in whole or in part, to methods of, or the performance of, abortions or involuntary sterilization as a means of family planning?

No

20. <u>FY 1986 Continuing Resolution</u>. Is the assistance being made available to any organization or program which has been determined as supporting or participating in the management of a program of coercive abortion on involuntary sterilization?

No.

If assistance is from the population functional account, are any of the funds to be made available to family planning projects which do not offer, either directly or through referral to or information about access to, a broad range of family planning methods and services?

No.

21. <u>FY 1986 Continuing Resolution Sec. 529</u>. Has the recipient country been determined by the president to have engaged in a consistent pattern of opposition to the foreign policy of the United States?

No.

22. <u>FY 1986 Continuing Resolution Sec. 513</u>. Has the duly elected Head of Government of the country been deposed by military coup or decree?

No

b. <u>FUNDING SOURCE CRITERIA FOR COUNTRY ELIGIBILITY</u>

1. <u>Development Assistance Country Criteria</u>

<u>FAA Sec. 116</u>. Has the Department of State determined that this government has engaged in a consistent pattern of gross violations of internationally recognized human rights? If so, can it be demonstrated that comtemplated assistance will directly benefit the needy?

No.

2. <u>Economic Support Fund Country Criteria</u>

<u>FAA Sec. 502b</u>. Has it been determined that the country has engaged in a consistent pattern of gross violations of internationally recognized human rights? If so, has the country made such significant improvements in its human rights record that furnishing such assistance is in the national interest?

No.

ANNEX C

DESCRIPTION OF MAJOR USAID/GOS LOCAL CURRENCY

Despite a commodity program that has run approximately $170 million per year, resulting local currency generations are considerably less than calculations would show. In addition to arrearages, problems in GOS transfer of funds, poor Bank of Sudan bookkeeping practices and in FY 1985 the USG decision to hold (still undisbursed) $50 million for repayment to the IMF have all contributed to a lack of counterpart generation. An accounting of December 31, 1985 of balances of the special accounts of both Ex/Im Bank and the Bank of Sudan shows the amounts which GOS have been able to make.

ACCOUNT NO.	TITLE OF ACCOUNT	BALANCE
330 X/M	CIP VI B	LS 5,703,106.00
335 X/M	CIP VI A (2.50)	LS 107,712,789.26
336 X/M	CIP VI A (0.80)	LS 20,270,129.74
5001 X/M	PL 480 Title I -- FY 84	313,588.00
6001 X/M	PL 480 Title III	42,170,827.00
6002 X/M	PL 480 Title I FY 85 (I)	1,000,653.00
6003 X/M	PL 480 Title I FY 85 (II)	226,805.00
6004 X/M	PL 480 Title I FY 85 (III)	669,090.00
02-12-274 BOS	PL 480 Title III	29,616,538.26
02-12-297 BOS	CIP II	921,806.51
02-12-329 BOS	CIP III	1,118,564.83
02-12-333 BOS	CIP IV	272,515.51
02-12-432 BOS	CIP VI B	439,098.47
TOTAL AVAILABLE LOCAL CURRENCIES:		210,435,511.58

USAID's development strategy, and more recently its relief program, have come to depend heavily on the Local Currency program.

Governing Policies.

Generation and use of local currency under the CIP are governed by Sec. 609 of the FAA (as amended). Local currency proceeds generated from the CIP are to be programmed for developmental purposes (and limited support for the USAID mission). Titles I and III govern the generation and use of PL 480 local currencies for their respective programs. While the legislation also speaks of use of proceeds for development purposes, the definition is clouded by the stipulation that "proceeds" will equal the highest legal exchange rate equivalent of the commodity. A discrepency, of course, occurs when the Host Country chooses to subsidize the commodity at resale.

General Practices for Joint Programming of Local Currencies

In general, Sudan's Three Year Investment Program, developed in cooperation with the World Bank for the Consultative Group meetings, governs decisions on the use of local currency for development funds. Top priority in programming U.S. generated local currency goes to approved or anticipated AID DA projects. Second priority goes for local currency activities from the GOS development budget that may be in support of DA projects but not included in them. Closely related, a third priority goes to activities under Sudan's budget that are outside the project portfolio but directly in support of AID's strategy. Following that are activities related to AID's strategy in support of other donors projects. Local currencies left over are either programmed as miscellaneous or left to be programmed following the semi-annual review. The greatest exception to these priorities has been programming of local currencies for the emergency relief effort. The magnitude of the effort is detailed below.

Program Issues:

Issue 1: Programming Local Currency Counterpart vs Proceeds

USAID has been grappling for several years with how to standardize local currency requirements and procedures across the PL 480 and CIP programs. However, there has historically been confusion concerning the nature, and more importantly the amount of local currency USAID should require to be put into the Special Account, particularly under the PL 480 programs. Section 103 (h) of PL 480 stipulates that "the President shall obtain rates of exchange applicable to the sale of commodities under such agreements which are not less favorable than the highest exchange rates legally obtainable in the respective countries and which are not less favorable than the highest of exchange rates obtainable by any other nation..."

However, Section 104 (b) (1) of the same act authorizes and directs the Secretary of Agriculture "to enter into agreements with such countries for the sale of agricultural commodities...and for the use of proceeds to carry out the purpose of this paragraph." Section 106 (b)(1) stipulates that "Agreements hereunder for the sale of agricultural commodities for dollars on credit terms shall include provisions to assure that the proceeds from the sale of the commodities in the recipient country are used for such economic development purposes as are agreed upon in the sales agreement or any amendment thereto..."

The contradiction occurs when there is a subsidy in the resale of the commodity. In that case the proceeds are not sufficient to meet the requirement of the highest legal exchange rate clause of PL 480. The highest rate of exchange provision is an important A.I.D. policy as well in all its programs.

Beginning with the FY 1986 Title I Program, USAID has added four Local Currency Provisions (see Attachment 1) which are an attempt to help assure that the optimal developmental impact is obtained from both the PL 480 programs and the CIP. These additional stipulations in the Program Agreements provide an implementable way of tracking the uses of proceeds while assuring that the highest exchange rate provisions work in favor of USAID's development portfolio.

Issue 2: Joint Programming and Disbursements

Reorganization of the GOS and changes in priorities and procedures have once again created the problem of how to program local currencies and how to get them released for the agreed upon activities. PL 480 has historically provided the greatest problem since the GOS practice was not to require beneficiaries to deposit local currencies soon after receipt of the commodity. Simultaneously GOS made local currencies available to cover all costs of handling before proceeds were deposited to the Special Account. Thus, the level of deposits always lagged.

Actual disbursements to the beneficiary projects had often been equally problematical. Approval passed through a myriad of offices each with its own special and unarticulated criteria for rejecting the transfer request or requiring additional information. Five new provisions to the PL 480 Agreement, coupled with two Annexes outlining agreed upon procedures, attached, are henceforth being incorporated into the Agreements. Once these are tested, USAID intends to standardize these and apply them to CIP as well subject to RLA approval and guidance.

Issue 3: Tracking

Central to improving the collection of local currency generations is a simplified tracking system for both PL 480 and CIP. Amounts due must be clearly established as well as the dates. The attached provisions on local currency stipulate that the amount and date of disbursement by CCC will control for the PL 480 programs. While not finalized, USAID intends to propose disbursement amounts and shipping dates to determine amounts and timing of GOS responsibility for local currency under the CIP.

Issue 4: Additionality

Because of the amount of local currencies requiring joint programming in relation to GOS overall budget, the concept of additionality has been problematic in the face of a budget deficit of close to LS 1 billion. Basically the GOS position has been that fallout from GOS devaluations or the difference between the 3.3 and 2.5 rates should go to covering the Government's serious budget deficit rather than adding onto additional development activities the Government believes it cannot afford. As a result, under the FY 1985 Program, GOS and AID/W concurred that GOS and AID would stipulate the exchange rate to be used (LS 3.3 = $ 1), which at the time was the commercial bank rate and the highest legal rate. The implications of this agreement were firstly, that in the face of any subsequent GOS devaluation, the joint programming for development activities would continue to acquire local currencies at the specified amount with any difference going to the GOS. Secondly, GOS further stipulated that of the 3.3 rate, only 2.5 would be strictly additional and the remaining 0.8 was to go for gross (replacement) investment for development, albeit jointly programmed by USAID.

USAID's position is that this arrangement was a one shot deal and that it would not continue under subsequent CIP's. Further, USAID has been adamant with the GOS that this practice could under no circumstances be applied to PL 480 programs where the legislation clearly requires the highest legal exchange rate for proceeds and joint programming. If USAID proceeds to an auction mechanism for CIP, an important side effect will be the positive impact on assuring the availability of the greatest amount of local currencies for development purposes.

Issue 5: Arrears

According to a recent USAID audit, GOS has never placed some LS 200 million as local currency counterpart into the Special Account.. Of this, the local currency equivalent of the first CIP, $39.5 million, was used for a general budget allocation. Local currencies equivalent to $38 million for the two cash grants also never generated counterpart in contravention to the Grant Agreement. Finally, beneficiaries of the various subsequent CIP's did not deposit approximately $ 176.6 million in counterpart. Among the worst offenders are:

Sudan Airways	2.7 million
Sudan Gezira Board	83.7 million
Rahad Ag. Corp.	24.8 million
GOS Agencies	8.5 million
Shell Oil	18.9 million
Sudanese Tractors	7.0 million

Identification of delinquent beneficiaries has been made more difficult because of poor Bank of Sudan accounting practices. Most notorious has been the "suspense account". Payments into the Bank of Sudan against Letters of Credit for CIP commodities are placed in a suspense account which have neither account statements in a current fashion nor accurate descriptions of source of deposits. USAID has therefore required that all deposits henceforth be made into the National Export Import Bank which has considerably better records and reputation for accuracy.

USAID is currently developing a Mission Order which will regularize the procedures and accountability for Local Currencies at which time specific proposals on how to handle the various delinguencies will be addressed. In the meantime, since the FY 1985 CIP, Covenants or CP's require that no previous CIP beneficiary currently considered in arrears to the Local Currency account can qualify for subsequent CIP allocations.

Summary of Local Currency Proceeds

(LS - Millions)

	Actual 81-84	84/85	85/86	86/87	Total
Generations					
Commodity Import Program	114.3	120.7	283.7	108.8	627.5
P.L. 480 Title III Program	85.2	36.0			121.2
P.L. 480 Title I Program		102.4	157.5	105.0	364.9
Total Generations	199.5	259.1	441.2	213.8	1,113.6
Balance Carried In		112.3	55.7	238.0	
Total Available	199.5	371.4	496.9	451.8	
Allocations					
A.I.D. Projects	52.3	33.6	93.7	76.0	255.6
GOS Development Projects		9.3	17.7	33.2	60.2
Emergency Food Programs	09	212.4	126.5	5.0	344.8
Mission Operations	34.0	60.4	21.0	21.5	136.9
Total Allocations	87.2	315.7	258.9	135.7	797.5
Balance (Unprogrammed)	112.3	55.7	238.0	316.1	316.1

Summary of CIP Counterpart Generations
(Minimum Generations in LS 000's)

			82/83	83/84	84/85	85/86
603-0	$100.0	mil	90,000			
604-0	$ 30.0	mil		54,000		
604-1	$ 18.	mil		32,400		
604-2	$ 12.25	mil			22,050	
605-0	$ 20.0	mil		36,000		
606A	$ 40.0	mil			132,000	
606B	$ 62.0	mil			111,600	
607	$ 18.0	mil			32,400	
608A	$ 40.0	mil				132,000
608B-0	$ 37.0	mil				122,100
608B-1	$ 34.0	mil				112,200
Total			90,000	122,400	298,050	366,300
Actual Deposits			35,878	55,079	71,861	N/A

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Summary of PL 480 Counterpart Generations
(Minimum Generations in LS 000's)

		82/83	83/84	84/85	85/86
Title III					
4/29/82	$80.0 mil	18,000			
6/13/83	$20.0 mil		26,000		
8/9/84	$20.0 mil			42,000	
Sub-Total		18,000	26.000	42,000	
Title I					
2/13/82	$ 5.0 mil	4,500			
1/20/83	$10 mil		13,000		
6/13/83	$ 4.5 mil		5,850		
12/10/83	$30.0 mil		39,000		
12/27/84	$25.0 mil			52,500	
1/9/85	$ 5.2 mil			10,920	
5/12/85	$30.5 mil				100,650
8/24/85	$17.0 mil				56,100
Sub-total		4,500	57,850	63,420	156,650
Total Title I & III		22,500	83,850	105,420	156,650
Actual Deposits		18,000	48,000	69,307	N/A

Sudanese Pound Expenditure from Special Account for Emergency Feeding Program, 1985

A. Commodities	
UNHCR	LS 750,000
B. Inland Transport	
Commodity Transport	58,538,562
Fuel Transport	3,500,000
Transport Support	13,500,000
WFP Transport	18,951,435
FANA Transport	8,140,027
Sub-Total	LS 202,630,024
C. Distribution	
General Distribution	LS 41,186,442
Supplementary Feeding	12,000,000
Sub-Total	LS 53,186,442
D. Other Sudanese Pound Expenditures	
Seed	LS 14,000,000
Port Charges	6,000,000
Sub-Total	LS 20,000,000
E. Total Sudanese Pound Expenditure	LS 276,566,466

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B. Inland Transport

Fuel (Gasoil) Purchase	$ 12,370,046
Commodity Transport	9,413,650
Transport Support	700,000
Airlift	12,000,000
Sub-Total	$ 34,483,696

C. Distribution

General Distribution	$544,211
Supplementary Feeding	$658,698
Sub-Total	$1,202,909

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* Includes ocean freight
** Includes 2,046 MT for WFP

D. Other Dollar Expenditures

Railroad (Spare Parts & Locomotives	$ 11,500,000
Port Equipment	1,000,000
Monitors and support	600,000
Sub-Total	$ 13,100,000

E. Total Dollar Expenditure $ 214,796,365

FY 1985 PL 480 Title II Summary

Dollar Expenditures

A. Commodities

	MT	Value*
Sorghum	527,000	$ 122,096,100
Wheat Flour	25,000	9,324,000
Vegetable Oil	13,365	14,990,860
Corn/Sorghum Milk	13,500	6,010,200
Non-Fat Dried Milk**	12,006	9,410,700
Beans	6,000	3,720,000
Bulgar	512	457,000
Sub-Total	597,383	$ 166,009,760

SC/

AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON D C 20523

JUN 2 1986

ACTION MEMORANDUM FOR THE ADMINISTRATOR

THRU: AA/PPC (Acting), Allyson B. Herrick ABH

FROM: AA/AFR, Mark L. Edelman MLE

SUBJECT: Sudan: Petroleum CIP Source/Origin Waiver to Code 935

Problem: Your approval is required to allow the procurement of petroleum, petroleum products and commodity-related services, including ocean freight, from countries included in the AID Geographic Code 935 for a FY 1986 Commodity Import Program for petroleum.

Background: In 1984, AID approved the first Petroleum Initiative CIP for $ 40 million, followed shortly afterwards by a second grant of $40 million from FY 1985 funds. Together with $5 million in Dutch financing and $ 60 million worth of in-kind Saudi crude oil, as well as tranched contributions by the GOS of about $7-8 million, sufficient supply was mobilized to get Sudan through the economically depressed, drought-stricken year.

As initially designed, the Petroleum Initiative was intended to regularize the GOS's procurement and distribution of petroleum. It was anticipated that AID funds ($40 million per annum) would be used primarily as a guaranty, leveraging the GOS's regular allocation of its own funds for petroleum procurement through open international tenders. At the end of the year, AID funds were to be used for a normal CIP procurement of petroleum. The GOS also agreed to numerous reforms within the petroleum sector. To get the Petroleum Initiative started, more of AID's funds were used for regular CIP petroleum procurements than initially planned.

With a more regular supply of fuel established, road transport costs were reduced by 15 percent on average, long and politically unpopular queues at filling stations were eliminated, and electrical power supply became more widely available and less erratic.

Substantial progress was also made in the tendering process. The return to the use of international competition reduced costs of petroleum to Sudan by about 30 percent. And as each tender has passed, these price advantages have become greater with tenders put out in a more timely fashion and issued to a larger number of prequalified suppliers.

The GOS made an extensive revision of petroleum prices in March of 1985, when all fuel prices were substantially increased. In June, when the next quarterly price review was to be undertaken, strong pressure by various interest groups was placed on the Ministry of Finance to reduce fuel prices (based largely on the notion that this would reduce the cost of transporting emergency food assistance supplies). In June, diesel prices were also reduced by 21 percent. However, it was a move with little solid support within the GOS and prices were restored to their original levels in 1986. With world prices coming down for most petroleum products, much of the subsidy in Sudan's pricing structure present at the onset of the Petroleum Initiative has been reduced. However, the process and reasoning behind pricing considerations will need continued attention in the future.

On May 11, 1986, AID/AFR staff met with State AS/AFR to determine what type of assistance might be provided to Sudan in time to represent a demonstration of support for the newly elected democratic government, at the same time recognizing USAID's lack of personnel to execute most types of assistance programs. State believes it imperative that AID provide petroleum immediately, on regular CIP terms without requiring formal leveraging of GOS funds or other covenants. It is especially necessary to demonstrate an alternative source of petroleum to other proffered in-kind donations, with terms that are credible. Additionally, the GOS has recently provided estimates that its petroleum supply would last only until June 1st for gas oil (diesel) and June 18th to 24th for gasoline, creating an acute shortage before new sources of petroleum could be received. Further, one of AID's primary objectives in providing petroleum to Sudan has been encouraging Sudan to use open international competition in procurement with its own funds. While this tranche is not fully integrated into the Petroleum Initiative, it is nevertheless closely related, particularly in Sudanese perceptions. Although formal determinations have not yet been made, there is a likelihood than the GOS will need to use its own funds for some petroleum procurements this year. While it is inappropriate under current circumstances for AID to formally require use of international competition for the expenditure of GOS funds, we believe that approving use of Code 935 and international tendering for procurement here will have a strong effect on encouraging GOS use of open international tendering with its own funds. Restriction of competition to Code 941 countries would substantially damage our credibility with past reforms and be inconsistent with our overall program thrust.

Justification: To achieve these purposes, a source/origin waiver allowing the purchase of petroleum products and commodity-related services, as well as ocean freight, from Geographic Code 935 sources will be necessary. This waiver is justified on several grounds. The primary rationale is "persuasive political considerations" as permitted by HB 1B, CH 5B4a(5). As described above, the State Department believes that it is imperative to provide petroleum immediately, on unrestricted terms. However, while not the primary grounds on which this waiver is based, HB 1B CH 5B4a(7) criteria which permit a waiver based on "such other circumstances as are critical to success of the program" are also relevant. As discussed above, even though there is no formal mechanism by which the program incorporates future GOS petroleum procurement procedures, it is an implicit part of this program to require full international competition. Finally, it is probable that the petroleum products purchased will be those for which there is the most urgent need. The only Code 941 sources from which Sudan could realistically purchase petroleum are Egypt and Kenya. However, it is not likely that sufficient quantities would be available on a timely basis to meet this need, which is a risk that this program can not accept. Also importantly, because Sudan's historical trading relationships have been with the Arabian Gulf States in Code 935, it is also unlikely that private Egyptian and Kenya suppliers (Code 941) would be competitive with them.

While Libya is currently included in Geographic Code 935, PPC is examining the feasibility of formally excluding it. Because of the possibility Libyan petroleum could be offered, Libya will be excluded from eligibility for this procurement, despite the waiver.

It is requested that exception be made to the policy of Code 941 ocean transport and that Code 935 be allowed. Handbook 1, Supplement B, Chapter 7B4a does not specifically list political considerations as criteria for a transportation waiver, but we believe that the same justifications that hold for the source/origin waiver to Code 935 for procurement of petroleum products and commodity-related services are appropriate for ocean freight as well. This transportation waiver does not affect the requirements for cargo preference, which still apply.

Once again, the primary justification for this source/origin waiver is to demonstrate support of the newly elected democratic government and help with balance of payments problems, which are significant political considerations.

Recommendation: That you approve a source/origin waiver from Code 941 to Code 935 (including Sudanese flag vessels eligible for ocean freight) to allow the procurement of up to $10 million of petroleum products and commodity-related services for a petroleum portion of the FY 1986 CIP (650-K-609A) by certifying that "exclusion of procurement from Free World countries other than the cooperating country and countries included in Code 941 would seriously impede attainment of U.S. foreign policy objectives and objectives of the foreign assistance program."

APPROVED: [signature]

DISAPPROVED: ____________

DATE: June 2, 1986

Clearances:

State/AF/E: JMartin	(draft)	Date: 5/29/86
AFR/PD/EAP: WWeinstein	(draft)	Date: 5/23/86
AFR/PD, LHausman	[signature]	Date: 5/30/86
AFR/EA, SMintz	[signature]	Date: 5/30/86
GC/AFR, BBryant	[signature]	Date: [illegible]
GC/CCM, KFries	[signature]	Date: [illegible]
PPC/PB, HHandler	[signature]	Date: [illegible]
SER/AAM/OS, SDean	(draft)	Date: 5/28/86
DAA/AFR/ESA, LSaiers	[signature]	Date: 5/30/86
AFR/DP,J Patterson	[signature]	Date: 5/30/86
GC, HFry	[signature]	Date: 6/2/86

DRAFTED: AFR/PD, TCornell/THarris:tfc:x78288:5/23/86:2570J