CLASSIFICATION:

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AID 1120-1		
PAAD	DEPARTMENT OF STATE AGENCY FOR INTERNATIONAL DEVELOPMENT PROGRAM ASSISTANCE APPROVAL DOCUMENT	1. PAAD NO. 669-K-605 Amendment No. 1 2. COUNTRY Liberia PD-BBG 015 3. CATEGORY Cash Transfer Amendment No. 1 4. DATE January 17, 1983

5. TO: M. Peter McPherson Administrator	6. OYB CHANGE NO. N/A 8. OYB INCREASE None
7. FROM: Francis Ruddy Assistant Administrator for Africa	Budget Plan Code GESA-8-31669-KG31
9. APPROVAL REQUESTED FOR COMMITMENT OF: $ 24,000,000 ($32,000,000 total)	10. APPROPRIATION - ALLOTMENT APP No. 72-1121037 Allot. No. 337-61-69-00-00-50-21

11. TYPE FUNDING	12. LOCAL CURRENCY ARRANGEMENT	13. ESTIMATED DELIVERY PERIOD	14. TRANSACTION ELIGIBILITY DATE
☐ LOAN ☒ GRANT	☐ INFORMAL ☐ FORMAL ☒ NONE	1/28/82 thru 9/30/83	

15. COMMODITIES FINANCED

N/A

16. PERMITTED SOURCE	17. ESTIMATED SOURCE
U.S. only:	U.S.:
Limited F.W.:	Industrialized Countries:
Free World:	Local:
Cash: $24,000,000 ($32,000,000 total)	Other:

18. SUMMARY DESCRIPTION

The purpose of this grant amendment is to help the Government of Liberia (GOL) deal with its continuing fiscal and public sector balance of payments problems by making available resources needed for offshore dollar balances and budgetary support over the current U.S. FY 1983.

The proposed total grant to be made available in FY 1983 is $32,000,000, of which $24,000,000 is authorized in this PAAD amendment. The first tranche of $8,000,000 was authorized and disbursed in October 1982 under the original PAAD in order to enable the GOL to reduce the IMF "net credit to government" ceiling from the then $188 million to $180 million by October 29, 1982, and thereby meet IMF Standby Agreement performance criteria. This amendment in the amount of $24,000,000 will assist the GOL to continue to meet its immediate financial obligations. An initial disbursement of up to $12 million will be made under this amendment in January 1983. Subsequent disbursements will be made subject to the availability of ESF funds in FY 1983.

Provision of this program grant amendment will further strengthen U.S./Liberia relations by once again illustrating the ability of the U.S. to respond effectively during Liberia's time of crisis, and reconfirm the wisdom of Liberia's policy of maintaining close ties with the free world's financial and economic system.

19. CLEARANCES	20. ACTION
AFR/DP:H.Johnson HJ GC/AID:C.Van Orman CVO AFR/CCWA:J.Johnson GC/AFR:D.Robertson AFR/PD:N.Cohen DAA/AFR:F.Correl M/FM/PAD:W.McKeel ESD for AA/PPC:J.Bolton	☒ APPROVED ☐ DISAPPROVED M. Peter McPherson — 1/26/83 AUTHORIZED SIGNATURE — DATE Administrator TITLE

CLASSIFICATION:

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ACTION MEMORANDUM FOR THE ADMINISTRATOR

FROM : Assistant Administrator - Africa Bureau, F. S. Ruddy

SUBJECT : Liberia Program Grant (669-K-605)

Problem: Your approval is requested to authorize a $24 million increase for the program grant (cash) to Liberia, to a total of $32 million as presented in the FY 83 CP. $12 million will be obligated at this time.

Discussion: During the period between August 1980 and July 1982 AID provided the Government of Liberia (GOL) program grants totaling $72 million to assist in its economic recovery and stabilization. The planned level of program grant assistance for FY 1983 as shown in the Congressional Presentation is $32 million. In October 1982 we authorized and disbursed $8 million. At this time firm FY 83 OYB program grant allotments have not yet been fixed for specific countries but an interim apportionment for Liberia of $12 million has been made which increases the program grant level from $8 million to $20 million for FY 1983. For program purposes, we recommend that the balance of the $24 million ($32 million CP level less $8 million obligated October 28, 1982) be authorized at this time. If additional apportionments are made available, subsequent disbursements will be made in April and June of 1983.

Liberia's economic difficulties began in the 1970s with the worldwide recession and the resulting decline in demand for Liberia's principal exports. This economic decline was accelerated in April 1980 by the military coup which lead to a fiscal crisis. However, the GOL is taking steps to overcome its problems. A series of measures was adopted to control government expenditures, reduce subsidies and increase revenues. The government currently is participating in and adhering to a SDR 55 million ($59 million) IMF Standby Stabilization Agreement for GOL FY 1982-1983. Since the inception of the GOL/IMF Standby program in 1980, cumulative IMF assistance (including the FY 1982/83 program) has amounted to SDR 142.5 million. In addition, Liberia has drawn $27 million under the IMF's Compensatory Financing Facility (CFF). Liberia is the only country in Africa to meet IMF targets for nine consecutive quarters. Budget deficits have fallen from $110.5 million in 1980/81 to $106.5 million in 1981/82, and the projected deficit for 1982/83 is about $85 million.

The IMF review team that visited Liberia in November-December 1982 recommended that, given additional undertakings by the GOL and upon the GOL's meeting the January 29, 1983, performance targets under the Standby Agreement, $32.1 million be released to the GOL in late February.

On December 1, 1982, Head of State Doe addressed the nation and shared with the Liberian people the nature of the country's problems and an explanation of the government's planned actions to correct the present imbalance in the budget. Among the measures announced in the speech were across-the-board cuts in government and public corporation salaries ranging from 16.66 percent to 25 percent or a 17 percent reduction in public sector spending on wages. The GOL estimates that salary cuts of this magnitude, effective January 1, 1983, will result in a reduction of $2.25 million per month in GOL spending, or a $27-million-a-year savings, as well as savings of $3.6 million per year for publicly held corporations. These salary cuts will affect virtually all categories of employees. Also announced were greater efforts to increase revenues through more efficient collecton of taxes and customs duties. The GOL hopes to accomplish this with stepped-up enforcement of corporate income, customs, excise and other taxes.

This Grant Amendment is designed to assist Liberia through its period of crisis. It is not an open-ended commitment to the country. The tranches of this Amendment will be disbursed when Liberia satisfactorily complies in each case with the Conditions Precedent in the original grant. These conditions are directly related to and supportive of Standby terms and, further, support the efforts of U.S. advisors financed under two AID projects. They are consistent with recommendations made by Elliot Berg in his February 1982 report, "The Liberian Crisis and an Appropriate U.S. Response."

Although the GOL has satisfactorily met the Conditions Precedent for prior disbursements of funds, the present requirement for generation of counterpart funds needs to be reconsidered. The requirement that counterpart funds be generated under <u>all</u> applications of ESF flows is counterproductive, given the present and foreseeable conditions of the GOL's financial situation.

The counterpart concept was developed in view of the inconvertibility of locally held dollars into dollars to be used to meet foreign exchange obligations offshore. This situation exists because of the National Bank of Liberia's inability to transfer funds out of the country, because of insufficient offshore balances in its corresponding bank account (Morgan Guaranty, N.Y.). It was thought that since earlier ESF grants had helped pay oil import bills, sales proceeds of oil on the local market would generate inconvertible, locally held dollars, which then could be used to help fund development activities, in a similar fashion to counterpart generations under the PL 480 Title I program or from traditional CIP programs using ESF financing.

The assumptions underlying application of counterpart generation concepts have proved to be partially incorrect. When ESF funds were used to finance crude oil imports from offshore, domestic oil sales did not always generate an equivalent amount of receipts. The principal factor causing the shortfall was "leakages" in the system, largely attributable to inability of major purchasers to pay the Liberia Petroleum Refinery Corporation (LPRC), which currently has receivables outstanding totaling $42.3 million.

Further, assumptions regarding counterpart generations proved totally invalid when ESF funds were used to service external debt or were used to import cash to meet government payrolls. In these cases, no counterpart was generated at all. Accordingly, to meet AID requirements the GOL had to obtain counterpart equivalent from already inadequate general revenues, thus exacerbating its severe liquidity problem. The GOL, in effect, had to trade internal foreign exchange relief against domestic revenue and budgetary hardships. As the recent CDSS team pointed out, to require counterpart deposit and release in the absence of genuine sales proceeds to the GOL (not just intra-governmental transfers) is to require deficit financing by the GOL and makes it more difficult to comply with IMF ceilings for net credit to the government.

Therefore, we will drop the counterpart requirement from this Amendment. However, we will utilize the leverage offered by past agreement governing generation of the $38.5 million as a means of urging further reforms on the GOL in exchange for forgiveness of all or part of this outstanding balance. These future negotiations will require the GOL's continued implementation of measures to improve its financial position. That portion of the balance not forgiven, with P.L. 480 counterpart, will continue to be allocated to the development budget.

To replace the Condition Precedent governing deposit of counterpart into the Special Account, AID will add a new condition requiring the GOL to spend the full amount planned in its annual development budgets on certain priority projects to be agreed between the United States and the Government of Liberia.

<u>Conditions Precedent</u>: Section 2 B(7) of The Conditions Precedent to Additional Disbursements, p. 3, of the original Grant Agreement will be deleted and replaced with the following:

> "That the GOL continue to meet its locally funded share of development projects as may be agreed between the GOL and USAID, through timely and adequate disbursements of funds for salaries, other services, materials, and supplies and equipment associated with these projects, and that no such funds will be transferred to other expenditure codes."

All other Conditions Precedent and Convenants remain the same except that in Section 2, the "Conditions Precedent for Additional Disbursement" will now become "Conditions Precedent for the three disbursements proposed in this amendment."

<u>Recommendation</u>: That you sign the attached PAAD authorizing an amendment to the program grant to Liberia for an additional $24 million.

Clearances:
AFR/DP:H. Johnson
AFR/CCWA:J. Johnson
GC/AFR:D. Robertson
AFR/PD:N. Cohen
DAA/AFR:F. Correl
M/FM/PAD:W. McKeel
AA/PPC:J. Bolton
GC/AID:C. Van Orman

I. Summary and Recommendations

Authorization of an amendment of a Program Grant (cash) to the Government of Liberia (GOL) in the amount of $24 million is recommended. Although this authorization amendment will increase the total authorization from $8 million to $32 million, which is the funding level shown in the FY83 congressional presentation, only $12 million will be disbursed at this time. This $12 million, to be disbursed no later than January 28, 1983, coupled with the $8 million disbursed on October 28, 1982, raises the disbursement level for FY83 to $20 million. The balance of the $32 million, may be made available at a later date, subject to the availability of funds and the AID operational year budget allotment process. Mission understands that it cannot issue any amendments to Grant Agreement 669-K-605 in excess of $20 million without additional allotment of funds from AID/W and specific AID/W approval.

A provision of the original Grant Agreement requiring the GOL to deposit 100 percent equivalent of ESF funds in Liberian-held dollars as counterpart funds into a special account at the National Bank of Liberia is modified by this Amendment. Under the current agreement, only $8 million in ESF has been disbursed thus far (October 28, 1982). The GOL was given ninety (90) days from the date of disbursement to generate the equal amount in counterpart funds, to deposit these into a special account, and to apply these funds to selected development activities. This is still ongoing. In the aggregate, under ESF grants III, IV and V, the GOL thus far has been required to generate $68 million in counterpart funds. As of the latest GOL accounting figures (March 1982), it had accounted for only $16.5 million in disbursements. The difference of $51.5 million is accounted for partially by (a) the long accounting lag on the part of the GOL; (b) the fact that $13 million was used for debt services and did not generate any counterpart funds; and (c) "leakages" out of the system when ESF was applied to oil bills, a situation that is illustrated by a $42.3 million "accounts receivable" item at the Liberia Petroleum Refinery Company (LPRC). Such counterpart generation no longer will be required. Instead, the GOL will be required to disburse its share of the local costs of approved development projects included in annual GOL development budgets, and to ensure that no funds are transferred from these projects to other expenditure codes. Such activities may include new as well as ongoing activities, so long as they are in agreement with and adhere to IMF development budget restrictions. As appropriate and as part of its policy dialogue, USAID may utilize the prospect of forgiveness of part of the outstanding $51.5 million in exchange for needed GOL policy decisions.

II. Summary Justification

Liberia's economic difficulties began in the 1970s with the worldwide recession and the resulting decline in demand for Liberia's principal exports and shipping industry. This led to decreasing government revenues, while the costs and levels of the country's imports, especially oil and foodstuffs, increased. Expansionary domestic policies, including the Development Plan of 1976-1980 and the construction activities associated with the 1979 OAU Conference, were financed by government borrowings, further aggravating the situation. Political tensions, always present, erupted in the form of the 1979 rice riots. These riots led to the loss of business confidence, significant capital flight and a reduction in foreign and domestic investment. As a result, government revenues fell sharply in the remainder of [illegible].

The economic situation in Liberia, although serious, was thought to be a manageable fiscal problem until the April 1980 military takeover. The immediate reaction of the business community, both local and international, to the coup was expressed by massive capital flight, tightening or withdrawal of credit, and delayed or cancelled investments. The unexpected reduction in revenues turned the previously manageable problem into a fiscal crisis and threatened the stability of the country.

The inexperienced leaders of the coup found the state of Liberia's economy to be in worse shape than expected. The treasury was empty. The level of government indebtedness in June 1980 showed external debts of \$727 million, and internal debts of \$58.4 million, with a debt service of \$76 million or 34.5 percent of expected revenue. The new government's actions compounded the problem when it substantially increased the minimum public sector wages, with the lowest levels of government workers receiving a 100 percent increase and military and security forces receiving a 200 percent increase. Personnel ceiling levels also were raised substantially. The GOL's recurrent costs budget, excluding debt service, now earmarks approximately 85 percent for salaries.

The GOL is taking steps to overcome its problems. A series of measures was adopted to control government expenditures, reduce subsidies and increase revenues. The government currently is participating in and adhering to a SDR 55 million (\$59 million) IMF Standby Stabilization Agreement for GOL FY 1982-1983. Since the inception of the GOL/IMF Standby Program in 1980, cumulative IMF assistance (including the FY 1982/83 program) has amounted to SDR

142.5 million. In addition, Liberia has drawn $27 million under the IMF's Compensatory Financing Facility (CFF). Liberia is the only country in Africa to meet IMF targets for nine consecutive quarters. Budget deficits have fallen from $110.5 million in 1980/81 to $[illegible] million in 1981/82, and the projected deficit for 1982/83 is about $85 million. Debt arrearages, which were substantially controlled under prior Standbys, recently have begun to accumulate again.

The IMF review team that visited Liberia in November-December 1982 reviewed GOL performance under the current Standby Agreement. During this review process the GOL agreed: (a) to implement the newly announced Salary Readjustment Scheme, which when fully operational will reduce the annual GOL salary bill by 17 percent; (b) to clear up external debt service arrears and not allow new arrears to build up during the remainder of the fiscal year; (c) to reduce the local contribution to the FY 1982-1983 Development budget by $3.7 million; (d) to revise revenue forecasts by $13 million for FY 1982-1983; and (e) to conduct an audit of the Liberia Petroleum Refinery Company (LPRC) relative to its offshore foreign exchange position and to initiate efforts to collect the $42.3 million in "accounts receivable" due the refinery. The cumulative effect of reduced recurrent and development expenditures and a downward revision of the revenue forecast amounts to a budgetary improvement of $21 million on an annual basis. The IMF team recommended that given these additional undertakings, and upon the GOL's meeting the January 29, 1983, performance targets under the Standby Agreement, $32.1 million (representing the November and March tranches) be released to the GOL in late February. The team also recommended that the ceiling in net credit to government by the public banks be raised from $30 million to $32 million in the 12-month period ending June 30, 1983.

In spite of the effects of these recent policies and actions by the GOL, the economic problems persist even though the fiscal problems are being addressed. This is because of the following reasons: (1) Dependency of Liberia on international markets and the fact that the prices it receives for its exports continue to decline; (2) the worldwide recession and the stagnant rate of growth and investments; (3) the continued necessity of GOL offshore bridge financing at high interest rates; (4) a continued need for a high level of imports, including foodstuffs and oil; (5) the current lack of an energy conservation program; and (6) despite progress made over the past two years under the current IMF stabilization program to restore the GOL's fiscal position, the confidence of the domestic and international business communities in the country's economy has yet to be restored.

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The United States has important historic and strategic interests in Liberia, U.S. Government communication facilities, and almost $300 million in private sector investment. Because of the historical "special relationship" between the United States and Liberia, the U.S. Government's position on the political and economic changes now taking place in Liberia will have a critical impact on these changes, the future of U.S. interests in the country, and the actions of other donors and the international business community toward Liberia. If, with U.S. support and assistance, Liberia can revive its economy and continue to grow, U.S. interests in and relations with Liberia will be strengthened. If Liberia is unable to revive its present economic system and believes that lack of support from its traditional ally is even a partial reason for this failure, the Liberian Government may attempt more radical solutions to its present problems. Under these conditions, U.S. political, strategic and economic interests in Liberia might suffer.

This Grant Amendment is designed to assist Liberia through this period of crisis. It is not an open-ended commitment to the country. The tranches of this Amendment will be disbursed when Liberia satisfactorily complies in each case with the Conditions Precedent in the original grant. These conditions are directly related to and supportive of Standby terms and, further, support the efforts of U.S. advisors financed under two DA projects and of the IBRD. Many of them, too, are consistent with recommendations made by Elliot Berg in his February 1982 report, "The Liberian Crisis and an Appropriate U.S. Response," on tightening expenditure control, the parastatals and supporting the IMF.

The Conditions Precedent are as follows:

"1. That the Government has installed or is maintaining an operative system, updated monthly, to project for the next twelve (12) months, estimates of the availabilities and requirements of offshore public sector funds;

2. That the Government has reviewed or is reviewing its system of expenditure approvals and controls, with particular emphasis on extra-budgetary expenditures and budgetary transfers, identified and implemented necessary measures for improvement, and formulated specific criteria for prioritizing expenditures in the event of shortfalls in revenue availabilities;

3. That the Government is continuing its efforts to increase revenue generation through improved and increased collection of taxes, fees and other income sources, and continuing to install new security controls to safeguard revenues collected;

4. That the Government has caused or is causing to be carried out an independent audit(s) of the personnel expenditures of selected Government Ministries and Agencies;

5. That the Government is continuing its efforts to reduce or settle bills due to public corporations; and

6. That the Government has undertaken or is undertaking, a review of its public investment program as set forth in the second four-year Development Plan for 1981-85, in order to bring proposed investment more in line with the 1982/83 Development Budget ceiling and anticipated Development Budget levels in the remainder of the Plan period. In so doing, the Government should develop and apply criteria for determining priority projects for inclusion in its annual Development Budgets."

III. Economic Development in Liberia

The general economic development situation in Liberia basically remains the same as that described in the original FY 1983 PAAD. Since that PAAD was authorized in October 1982, however, several GOL actions have occurred that provide further evidence of its serious attempts to deal with its economic problems.

On December 1, 1982, Head of State Doe addressed the nation and shared with the Liberian people the nature of the country's problems and an explanation of the government's planned actions to correct the present imbalance in the budget. Among the measures announced in the speech were across-the-board cuts in government and public corporation salaries ranging from 16.66 percent for those earning less than $750 per month to 20 percent for those in the $751 to $1,500-per-month bracket, and a 25 percent reduction for those earning more than $1,500 per month. Overall, this represents a 17 percent reduction in public sector spending on wages. The GOL estimates that salary cuts of this magnitude, effective January 1, 1983, will result in a reduction of $2.25 million per month in GOL spending, or a $27-million-a-year savings, as well as savings of $3.6 million per year, or $ .3 million per month for publicly held corporations. These salary cuts will affect virtually all categories of employees. Teachers, doctors and nurses are considered a special category and further studies are in progress to determine their salary status. The retirement of GOL employees aged 65 and older and of selected employees with more than 25 years of service also will be pursued.

Also announced were greater efforts to increase revenues through more efficient collection of taxes and customs duties. The GOL hopes to accomplish this with stepped-up enforcement of corporate income, customs, excise and other taxes, and the return of the timber stumpage tax collection from the Forest Development Authority to the Ministry of Finance. An energy-conservation strategy is being considered to help reduce oil imports, which currently account for approximately 31 percent of total imports. Foreign travel and per diem for government officials will be reduced, although further reduction is both feasible and desirable.* These measures are compatible with IMF and U.S. economic advice to the GOL.

Although these measures are unprecedented and courageous, they also are an overdue step in the right direction. However, they probably do not go far enough in eliminating the GOL's deficit problems. To date the GOL continues to rule out the possibility of much reducing the number of employees on its payroll. Head of State Doe has announced that the expected savings from the reduction in the oil bill would be considered for salary increases for doctors, nurses and teachers. The removal of the surcharge for all but luxury goods will result in a decline in government revenues of $2.5 million, which may or may not be offset by improved revenue collections and enforcement. These continued issues should be the focus for joint, coordinated attention

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* Even with a 25 percent reduction in the base rate, the GOL per diem for Washington, D.C. (including an 8 percent cost-of-living allowance) still amounts to $150 a day, twice the U.S. Government rate.

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by the USG and the IMF during the remainder of FY 1983 and during negotiations for the next Standby Agreement early this summer. (See Monrovia 12755.)

IV. Requirements for Assistance

A. Analysis

The original Program Assistance Approval Document for FY 1983 contains an in-depth analysis of the gap between the GOL's projected offshore income and expenditures. An updating of this analysis of Liberia's projected financial gap reflecting recent GOL economic policy decisions reveals public sector offshore expenditures of $219 million and receipts of $178.1 million (see attachment). This gap includes all expected IMF and ESF inputs through November 1983. This forecast shortfall and the continued GOL deficit position considers the recent steps taken to control expenditures and increase revenues. The projection may, in fact, be optimistic, since most observers of the Liberian economy expect earnings from maritime revenues and royalties and from salary taxes from the concessions to be down from the levels attained in previous years. The present financial situation of most of the concessions is poor, with several major ones, e.g. Firestone, negotiating with the Liberians at least either partially to close or to have the GOL take over their social welfare activities. LAMCO has just reduced its work force by 1,300 employees and other iron ore companies are in similarly dire straits. In addition, the shift in tax burden from corporate to individual income taxes and the cut in salary rates may result in lower tax revenues. The recent GOL decision, based on the IMF review exercise, to reduce the FY 1982-83 revenue forecast by $13 million reflects these developments.

The foreign commercial banking system is more and more cautious about lending to Liberia. The GOL's present credit rating entitles it to obtain little more than bridging loans to enable the economy to survive until the disbursement of the next IMF or ESF tranche. These loans are priced slightly higher than LIBOR.* The international commercial banks are increasingly concerned that the GOL remain current on interest payments, with its clearing arrearages, and with reducing their loan exposure to the country. No major assistance, with the exception of high-interest bridging loans, can be expected from them.

Further IMF assistance is dependent upon the GOL's continued compliance with its Standby Agreement. The level

* London Interbank Offered Rate

of future IMF assistance, however, will decline sharply, since the Liberians are rapidly reaching their SDR ceiling and the net flow of IMF funds to Liberia will decline with the subtraction of the costs of debt servicing. Compared to 1982/83 drawings of $59 million (55 million SDRs), it is expected that the net flow in 1983/1984 will be approximately 19.4 million SDRs ($20.9 million) and approximately 5 million SDRs ($6.0 million), in 1984/85. The IBRD is considering a structural readjustment loan directed to the public corporations, but this may not be available for 18 months, or until sometime in 1984. The amount of that loan still is to be determined. Whether other donors will come forward to replace declining IMF resources is unknown at present.

Other donors, chiefly West Germany, the EEC, the Netherlands and U.N. agencies have chosen to provide assistance to specific development projects. The other donors see the IMF and the United States as having the primary responsibility for aiding the GOL to surmount its fiscal crisis and so far have been unwilling to play a more active role. The UNDP, however, is sponsoring a donor pledging conference for Liberia in Geneva in May 1983. The conference may produce little additional program assistance for Liberia to use in recovery of its economy, but may generate additional project aid. Given this outlook, the next few years in Liberia will be ones of a continued low-growth environment and resource stringencies.

The proposed U.S. assistance provided by this Amendment to the Program Grant will help the GOL to overcome its ongoing fiscal and public sector balance of payments crises. The initial disbursement under this amendment will provide the resources needed to help meet the January 29, 1983 IMF ceiling on "net credit to government."

A recent calculation showed that in December the GOL already had exceeded the January level by about $20 million.* However, January traditionally has been a good revenue month and it is anticipated that in addition to increased revenue flows, the January ESF tranche will help enable the GOL to remain under this credit ceiling. Actual application of funds will help to clear up foreign payments arrears owed to U.S. commercial banks, for Paris Club prepayments, and to the IBRD/IDA, (see attachment).

The estimated public sector foreign exchange gap between the minimum required to meet Liberia's offshore commitments and the resources available by the end of January 1983 is estimated to be $13.2 million (see Attachment). The funds in this Grant Amendment, as part of the U.S.

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* This calculation was dated Dececember 15, 1982. As of December 30, 1982 the January 29 ceilings had been exceeded by $30 million.

FY 1983 assistance, are essential to Liberia's economic, financial and political stability.

The initial two ESF grants (FYs 1980 and 1981) implied the generation of counterpart funds, but did not spell out this requirement in the agreement documents, even though ESF II called for the creation of a "Special Account" at the National Bank of Liberia into which funds would be deposited. These, however, were not Conditions Precedent to Disbursement. ESF III and IV, however, still implied the generation of counterpart funds, but made evidence of the creation of a Special Account and the subsequent deposit of (counterpart) funds into it a Condition Precedent for "subsequent disbursements" under these grants. The GOL satisfied these disbursement requirements and conditions with periodic reports to USAID before each release or subsequent release of funds. In FY 1983, USAID has begun requiring the GOL to meet more specific Covenants and Conditions Precedent to disbursement. The Conditions Precedent and Covenants contained in the original FY 1983 Grant Agreement directly support the IMF revenue and expenditure provisions, IBRD proposals on the public corporations, and encourage the GOL to begin to plan and monitor its costs for payments of oil, external debt and salaries.

B. Tranches

The original PAAD stated that funds would be disbursed in four tranches throughout FY 1983. The first tranche, $8 million, was authorized and disbursed in October 1982. The second tranche - of $12 million - will occur in late January after the signing of this Amendment and satisfaction of Conditions Precedent, in time to meet the IMF-imposed "net credit to government" ceiling target on January 29. Subsequent disbursements are scheduled for April and June 1983.

C. Counterpart Generation and Special Account

Although the GOL has satisfactorily met the Conditions Precedent for prior disbursements of funds, the present requirement for generation of counterpart funds needs to be reconsidered. The requirement that counterpart funds be generated under all applications of ESF flows is counterproductive, given the present and foreseeable conditions of the GOL's financial situation.

The counterpart concept was developed in view of the inconvertibility of locally held dollars into dollars to be used to meet foreign exchange obligations offshore.

This situation exists because of the National Bank of Liberia's inability to transfer funds out of the country, following from insufficient offshore balances in its corresponding bank account (Morgan Guaranty, N.Y.). It was thought that since earlier ESF grants all had helped pay oil import bills, sales proceeds of oil on the local market would generate inconvertible, locally held dollars, which then could be used in turn to help fund development activities, in a similar fashion to counterpart generations under the PL 480 Title I program or from traditional CIP programs using ESF financing.

The assumptions underlying application of counterpart generation concepts have proved to be partially incorrect. When ESF funds were used to finance crude oil imports from offshore, domestic oil sales did not always generate an equivalent amount of receipts. The principal factor causing the shortfall was "leakages" in the system, largely attributable to inability of major purchasers to pay the Liberia Petroleum Refinery Corporation (LPRC), which currently has receivables outstanding totaling $42.3 million. For example, the Liberia Electricity Corporation (LEC) owes LPRC more than $14 million because its customers -- including the GOL and certain public corporations -- either do not have the cash available or will not pay for electricity consumed. Similarly, Petro-Chemical Industries (PCI) which supplies the GOL with gasoline for its vehicles, owes $8 million because it cannot be reimbursed, under the GOL's existing financial difficulties, for official consumption. The LPRC has launched a program to collect outstanding bills and to make further sales only for cash. It is not expected that government or public corporations can comply with either of these requirements given the continuing liquidity crisis.

Further, assumptions regarding counterpart generations proved totally invalid when ESF funds were used to service external debt or were used to import cash to meet government payrolls. In these cases, no counterpart was generated at all. Accordingly, to meet USAID requirements the GOL had to obtain counterpart equivalent from already inadequate general revenues, thus exacerbating its severe liquidity problem. The GOL, in effect, had to trade internal foreign exchange relief against domestic revenue and budgetary hardships. As the recent CDSS team pointed out, to require counterpart deposit and release in the absence of genuine sales proceeds to the GOL (not just intra-governmental transfers) is to require deficit financing by the GOL and makes it more difficult to comply with IMF ceilings for net credit to government.

To date the GOL has been required to generate a total of $68 million in counterpart funds under four previous ESF grants and the initial October tranche of the FY 1983 grant. Of this amount, $13 million went for internal debt service and could not generate any counterpart, leaving $55 million in "real" generations. As of the latest GOL accounting (data is available only through March 1982) $16.5 million in counterpart has been disbursed for development spending from the Special Account since FY 1981. The outstanding balance of $38.5 million either is still being generated or deposited, or has been lost through leakages.

After reviewing the counterpart and Special Account situations as they relate to the ESF grants, USAID/Liberia was confronted with two choices: (1) Continue the counterpart and Special Account requirements as they currently exist in the Conditions Precedent of the Grant Agreement, in spite of the government's difficulties in meeting them; or (2) Develop alternative means to ensure the adequate disbursement of local funds for development purposes without further exacerbating the GOL's financial difficulties. The continuation of the counterpart requirement no longer is considered to be a viable option at the present time. The current counterpart requirement places a burden on the GOL's finances and jeopardizes the Government's ability to remain within the IMF's Standby Agreement levels. In fact, the GOL would have to borrow from the National Bank in order to meet the ESF counterpart requirements. Such a move would counter the IMF Standby Agreement. Managing counterpart deposits, especially given the "leakage" problem, is a heavy financial, programmatic and administrative burden on both the GOL and USAID, which is not justified, in our view, by the questionable benefits, developmental or other, derived from these deposits.

Therefore, USAID proposes to drop the counterpart requirement from this Amendment. However, we will utilize the leverage offered by past agreements governing generation of the $38.5 million as a means of urging further reforms on the GOL in exchange for forgiveness of all or part of this outstanding balance. These future negotiations will cover the GOL's continuing to implement measures to improve its financial position. That portion of the balance not forgiven, with P.L. 480 counterpart, will continue to be allocated to the development budget.

To replace the Condition Precedent governing deposit of counterpart into the Special Account, the USAID will add a new condition requiring the GOL to spend the full amount planned in annual development budgets on certain priority projects to be agreed between the United States and the Government of Liberia.

D. Conditions Precedent

Section 2 B(7) of The Conditions Precedent to Additional Disbursements, p. 3 of the original Grant Agreement will be deleted and replaced with the following:

> "That the GOL continue to meet its locally funded share of development projects as may be agreed between the GOL and USAID, through timely and adequate disbursements of funds for salaries, other services, materials, and supplies and equipment associated with these projects, and that no such funds will be transferred to other expenditure codes."

All other Conditions Precedent and Covenants remain the same except that in Section 2, the "Conditions Precedent for Additional Disbursement" will now become "Conditions Precedent for the three disbursements proposed in this amendment."

E. Reporting

The reporting requirements in the original Grant Agreement remain unchanged.

Dec 22, 1982

PRELIMINARY GOL PUBLIC SECTOR CASH FLOW PROJECTION
DEC. 1982 - NOV. 1983 ($MILLION)

	DEC	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEPT	OCT	NOV
SOURCES												
Opening Balance 1/	5.0											
Offshore Tax & Revenue Payments 2/	5.1	5.1	2.1	3.3	2.0	1.6	4.5	5.4	3.0	0.3	3.2	3.0
Public Sector Exports 3/	2.5	1.3	2.7	2.5	2.5	1.9	2.6	2.5	2.4	0.2	2.6	2.3
LPRC 4/	–	–	–	–	–	–	–	–	–	–	–	–
IMF Standby 5/	–	–	32.1	–	–	10.7	–	–	–	5.0	–	10.7
ESF	–	8.0	–	–	8.0	–	8.0	–	–	–	8.0	–
WACH	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5	.5
Miscellaneous	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Total Sources	14.1	15.9	38.4	7.3	14.0	15.7	16.6	9.4	6.9	7.0	15.3	17.5
USES												
Payroll Cash Imports 6/	7.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5
Crude & Product Imports 7/	5.8	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0
Debt Service 8/	–	14.0	12.0	4.2	4.2	4.2	4.2	6.0	6.0	6.0	6.0	6.0
Embassies & Scholarships	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5
IMF Charges		3.4	–	3.4	–	3.4	–	3.4	–	3.4	–	3.4
Miscellaneous		1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
NBL Advances (non-ad.)	(4.2)	–	–	–	–	–	–	–	–	–	–	–
NHSB Advances (non-ad)	(1.2)			(1.4)			(1.1)					
Total Uses	15.8	27.4	22.0	17.6	14.2	17.6	14.2	19.4	16.0	19.4	16.0	19.4
Surplus/shortfall	-1.7	-11.5	16.4	-10.3	-.2	-1.9	2.4	-10.0	-9.1	-12.4	-0.7	-1.9
Cumulative Surplus/shortfall	-1.7	-13.2	3.2	-7.1	-7.3	-9.2	-6.8	-16.8	-25.9	-38.3	-39.0	-40.9

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Footnotes

1/ Opening balance consists of $4.0 million available offshore by the NHSB and $1.0 million by the NBL.

2/ December revenues reflect $2.0 million of January payments which have been requested to be made earlier. Subsequent months offshore revenues reflect the strained conditions of the concessions depositing revenues in overseas GOL accounts.

3/ Public sector exports are slightly more optimistic than in the past, reflecting Liberia's expanded coffee export quota under the ICA.

4/ As concessions are likely to import their own fuel requirements in the absence of a firm oil financing facility, no foreign exchange deposits will be made to the refinery's offshore account.

5/ For FY 1983/84, it is assumed that an IMF standby agreement will be in force with disbursements scheduled as they were for FY 1982/83.

6/ Payroll cash imports from January onward reflect reduced need to import payroll cash because of the Salaries Readjustment scheme having become operational.

7/ Reflects largely product imports on a straight line average.

8/ Debt service calculations are as follows ($ m):

Debt Service due FY 82/83	75.0
Less IMF (listed separately)	-17.8
Other debt service due	57.2
(Monthly 4.76)	
Current arrears 14.0	
Implied payments thus far	-14.56
Other debt service remaining for FY	42.64
Assume debt service areas pd. in Jan '83	-14.00
Other debt service remaining Feb '83	28.64
Assume London Club payments in Feb '83	-12.00
Other debt service remaining for FY	16.64
March - June debt service (@ 4.16)	-16.64
	-0-

Debt figures do not include the approximately $26 million owed to the now defunct oil financing facility; it is assumed that this debt will be subject to a rescheduling arrangement.

ATTACHMENT 2

OUTSTANDING GOL DEBT ARREARS *
AS OF DECEMBER 1, 1982

A. Multilateral

IBRD		$ 2,350,194.46
IDA		21,940.00
ADB		1,887,478.70
OPEC Fund		68,997.63
BADEA		285,166.11
IFAD		1,660.48
Kuwaiti Fund		340,088.73
Saudi Fund		61,387.42
CDC		206,860.32
	SUBTOTAL	$ 5,223.773.85

B. Bilateral

USA		$ 2,187,273.60
UK (ECGD)		637,683.28
Italy (SACE)		279,262.59
Sweden (KKN)		264,258.05
Norway (GIEK)		340,003.89
Japan		8,081.70
France		1,345.50
	SUBTOTAL	$ 3,717,908.61

C. Commercial

Citibank		$ 441,080.28
Chase		4,630,000.00
Chemical Bank		1,498,590.06
Midland Bank		215,528.19
PK Baken (Lux.)		24,103.88
Taiyo Kobe Banks		970,758.45
	SUBTOTAL	$ 7,780,060.86
	TOTAL ARREARS	$ 16,721,743.32

*Exclusive of arrears on (now defunct) oil financing facility ($26 m.), London Club payments ($12 m.), Syndicate bridge loan ($4 m.)