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AEPRP ANALYSIS FOR THE REPUBLIC OF GUINEA

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PART I: CREDIT PROGRAM ANALYSIS

A. PRIVATE SECTOR ACCESS TO AND ANTICIPATED DEMAND FOR CREDIT

1. Nature and Scope of the Guinean Private Sector

The Guinean private sector is divided for purposes of this analysis into four categories of economic actors:

- farmers;
- traders;
- transporters; and
- small manufacturing and service enterprises.

These sectors have been in fact quite distinct until now. Only a handful of entrepreneurs have engaged on any significant scale in more than one of the above activities (typically a combination of trade and transport). There has been very little diversification within each sector (e.g. by product lines or transport routes) and from one to another, although the links between them are often well established. For example, today few of the leading traders own trucks: most lease them from established transporters (with men of confidence often accompanying the drivers). Transporters, on the other hand, do play an important if haphazard role in collecting agricultural produce and delivering it to regional markets and Conakry (as agents but also routinely as petty buyers and wholesalers). Part II of this study takes a closer look at the peculiarities of the Guinean private sector.

The liberal economic policies which are being designed and introduced in rapid succession have broadened the potential scope of each of the above sectors immensely, creating a wealth of opportunities. It can hardly be predicted how the private sector will react to the new freedom of enterprise, but expansion and diversification are certain to occur as steadily as the financial means and the necessary business experience are developed.

The natural leaders of the Guinean business community are long-time traders and transporters who operated for the most part in tolerated but confining illegality until the early 1980s when socialist restrictions began to be lightened, small plantation owners who have maintained or recovered productive land, and formerly expatriate Guineans who are returning to apply years of education and experience to the new situation, in some cases with savings and/or financial backing. They are not only pursuing activities which often seem ambitious in relation to the capacity of the current environment to support them and to their own resources and experience, but they are also helping to organize the institutional and policy framework for the private sector-led development which the Conte government is hoping to achieve in the long run. They are in effect "coming out into the open", through formal structures such as the Chamber of Commerce and an increasing variety of companies and associations, as well as informally, in direct communication with the government, donors and the new foreign-managed commercial banks.

This analysis and the proposed USAID credit program are ultimately concerned with rural sector-oriented private enterprise. However, it would be unfortunate (if not impossible) to discard any significant segment of the private sector from the design effort as being too far removed from the broadly-defined objectives stated in the terms of reference. Clearly, borrowers will have to qualify financially and on the basis of well-conceived conditions for the credit being offered, including conditions which may require specified uses of the funding. Beyond that, it is consistent with the political orientation and development potential of the country, as well as with the present unsophisticated structure but growing scope of the private sector, to let market forces determine where the credit will be applied as much as possible, once the basic features and conditions of the proposed USAID facilities have been established. Directly and indirectly, evolving market conditions and additional incentives and support can and will orient a growing portion of the stepped-up activity to markets outside of Conakry.

2. Access to credit

Since 1965, the private sector of the Guinean economy has had virtually no access to credit from the country's financial institutions, which were all 100 per cent state-owned, concentrated 95 per cent of their lending on the public and parastatal sectors, and have now all been permanently closed. The rural credit provided by the National Agricultural Development Bank (BNDA) was exclusively directed to state and party-controlled collective farming activities, and there have been no donor-supported agricultural credit programs until this past year (on a pilot basis). Private traders who have kept their businesses alive over the years succeeded in doing so partly because of the existence of "informal" credit arrangements (principally the supplier credit system discussed below). Private farmers, totally ignored (in many more ways than the lack of credit), gradually lost interest in cash crops and the cash economy, and for the most part drifted into subsistence farming.

There are at present four types of credit available in Guinea, other than micro-scale, purely informal forms of short-term credit (e.g. of the variety found in rural communities and extended family networks):

- o suppliers' credits, typically among merchants and transporters (i.e. and not between them and producers or consumers);
- o development project credits, thus far all sponsored by donors (only in the agricultural sector and for the most part still being designed);
- o commercial bank credits (which are only tentatively and experimentally being extended by the new banking system); and
- o donor-supplied hard currency credit lines (which cannot in principle be classified as "domestic credit") administered by the banks, although they are repayable in local currency (these are discussed in Section B below)

In certain cases, private Guineans also succeed in borrowing externally from commercial banks in West Africa as well as Europe with whom they are established depositors (partly as a result of the substantial exports of the Guinean parallel market). In addition, the government will be making one-time incentive payments to individuals leaving public sector employment. These are grants representing small amounts, expected to range from 50 to 100 times current monthly salaries (of $10 to $100 a month at the current exchange rate, thus a theoretical maximum payment of $10,000). They can nevertheless be entered into the equation as a source of financing, potentially for business activities, which will be available in the coming months.

Finally, it should be noted that traders regularly provide agents with cash advances to purchase merchandise, even in some cases unaccompanied transporters who regularly provide service to and from markets in neighbouring countries. Of late, leading merchants have contemplated unusually large transactions with more or less "independent" buyers in connection with the first season for coffee open to the private sector. In turn, certain merchants and service organizations (e.g. a building maintenance contractor) receive advances (typically hard currency for imports) from "modern sector" clients such as the mining companies to purchase supplies and commodities on their behalf.

Access to the first three types of credit mentionned above aree discussed in the following sections. In addition, the availability of different forms of credit within these categories is reviewed in Section B.1.

a. <u>Supplier's credits.</u>

This has been the principal source of credit for private businessmen in Guinea, and continues to play a major role where consumer goods are concerned. It is a relatively unsophisticated system, in most cases based on personal trust in the context of family ties and social connections, but appears to have been working reasonably effectively and ranges across national borders. Credit terms depend on the nature of the commodity traded and the volume of the transaction, and usually range from 2 to 6 months. Goods are supplied at a negotiated all-inclusive price, and interest is not separately charged. Indeed, there is rarely any documentation involved in the transaction which would highlight the cost of capital. Any sales proceeds above the contracted price constitute the local distributor's margin.

The supplier's credits are granted almost exclusively by large merchants based in Conakry and to a much lesser extent by the leading traders in Kankan and Labe, to smaller merchants (the "local distributors") in these centers and other markets in the interior (see Part II for further description of the networks). The local distributor's margins are typically quite small, and transport costs are a critical variable in the equation, particularly in light of the recent tripling of official fuel prices (which in turn amount to as little as 25 per cent of black market fuel prices in markets where weekly supplies to official fuel distributors can be exhausted in less than a day).

<u>Example</u>: A distributor of cement in Kissidougou turned over 12 tons in January-February, 1986 and recently held 32 tons for sale. The operation is structured as follows:

Supplier's price ex-Conakry	FG 41,000 per ton
Transport costs as charged	<u>FG 10,000 per ton</u>
Payable in three months	FG 51,000 per ton
Distributor's price (2650 per 50kg bag)	FG 53,000 per ton
Distributor's margin	4 per cent

In order to gain some control over the transport margin, merchants in regional market towns do take delivery in Conakry sometimes, usually for cash, but occasionally on the same loosely defined suppliers' credit terms minus the transport cost.

The local distributors act as both wholesalers and retailers in their respective markets and themselves extend credit to petty retailers in the open markets, to prominent villagers and others (this level of the credit system was not examined). They constitute the next "tier" in the commercial sector, after the market leaders of Conakry, Kankan and Labe, and they could become increasingly aggressive in controlling bulk transactions, from or even beyond the country's borders. This process could be accelerated with new forms of credit, technical assistance and mutual support.

It is quite likely that the suppliers credit system will grow in volume and sophistication, and eventually in combination with other sources of credit. Larger networks are being organized by leading groups in Conakry (e.g. the former PLC group with 120 distribution points and the Mutuelle des Commerçants representing 300 traders), which should raise the level of formality and diversity of the credit system. Increasing diversification of product lines (i.e. to production inputs) could result in due time in the extension of credit to producers (farmers and small enterprises) by leading wholesalers and local distributors. That this is desirable and likely to occur eventually is a basic hypothesis which this analysis and the proposed USAID credit program are to address.

b. Development project credits

Credits will soon be available beyond pilot activities and in an organized and controlled manner to participants in certain specific agricultural development projects. The leading program is the $6 million credit component of the IBRD-funded PAG scheme in the Forest Region, which will supply one-year loans to participating farmers for agricultural inputs, and three-to-five year loans for equipment procurement and construction expenses. Interest is expected to be charged to the borrowers at 10 per cent per annum, and 80 per cent of the credit budget is available in foreign currency. Private farmers will also be eligible for credit in the CCCE/EDF-funded cotton project in Siguiri district and perhaps the UNDP/FAO produce project at Dalaba.

Although these projects have the advantage of professional management, and provide training and extension services, they would only cover a fraction of the rural population. The bulk of food and cash crop production occurs outside the project zones. However, it is difficult to envision producer-oriented credit programs outside of projects such as these, at least under present conditions. Two issues which are frequently being discussed in Guinea with respect to agricultural/rural credit are summarized below.

- It is critical that a legal framework be established for the creation of rural savings institutions (whether sponsored or run by local government institutions or not) as well as for rural borrowing units, such as cooperatives and other registered legal entities. This would strengthen prospects for commercial bank lending in the rural sector: since only one bank has thus far planned to establish branches outside of Conakry, any development which tends to better label and organize borrowers will raise the likelihood of Conakry-based lending to farmers.

- Given the nature of agricultural lending activities, it may be entirely appropriate to establish a specialized national development finance institution in this area once basic groundwork has been accomplished (e.g. restructuring the Ministry of Rural Development, developing a basic credit market in the commercial banking sector, evaluating the initial results of the above-mentionned programs' credit components and the experience of the proposed USAID program, etc.). It is unlikely that such an institution would be established within the next two years, but some donors have expressed a strong interest in supporting an initiative in this area as the new environment matures.

c. <u>Commercial Bank Credits</u>

(i) <u>Composition of the banking sector</u>

The banking sector has been completely restructured. All state banks were officially closed on December 22, 1985 and currently there are four banks in operation (of which the three principal ones were very recently established):

The <u>Banque Internationale pour l'Afrique de l'Ouest en Guinee (BIAG)</u> opened in August 1985. BIAG is a joint venture between the Guinean government (51%), the BIAO group (34%), and the Geneva-based Societe Financiere pour les Investissements et le Developpement en Afrique (SIFIDA 15%).

The <u>Banque Internationale pour le Credit et l'Industrie en Guinee (BICIGUI)</u>, which opened in January 1986. Current shareholders in this joint venture are:

- the Guinean government (50.7%) financed by the World Bank and European Development Bank;
- the Societe Financiere des Pays d'Outre Mer (SFOM) led by the Banque Nationale de Paris and including Banque Bruxelles-Lambert and Dresdner Bank (20%); and
- foreign assistance institutions (29.3%), now including IFC, CCCE, EDF and DEG. ADB is also expected to become a shareholder.

BICIGUI is managed by BNP under a management contract. Unlike the other banks, BICIGUI is committed to opening branches outside of Conakry, beginning with at least Kamsar, Labe and Fria in 1986 and branches in other regional capitals in succeding years. Premises have been secured in Labe and renovation is expected to begin shortly. BICIGUI has become the manager of World Bank and EDF credit lines for small and medium enterprises and will co-manage a proposed CCCE credit line with the other banks.

The Societe Generale de Banque en Guinee (SGB) also opened in January, 1986. It is 45% owned by private Guinean shareholders and 55% by European banks led by the Societe Generale, together with Credit Suisse, Banca Nacionale del Lavoro and Bayerische Vereinsbank. Its local partnership with private investors may well give it short-term advantages for lending opportunities both to and through its shareholders. SGBG is managed by the Societe Generale under a management contract.

Finally, Dar-El-Mal-Islami (DMI) was established in 1983 as a joint venture between the Guinean government and the Saudi-owned Islamic banking group. Shares were also issued to private Guineans. Seen from its balance sheet, it narrowly escaped being closed along with other state banks in 1985. Presumably other considerations led to its continued operations. It is unlikely that the bank would participate in the proposed USAID program, sinc it operates according to Islamic banking practices.

(ii) Current bank lending activities and funding bases

The new commmercial banks are just beginning to extend credit to the private sector, albeit in very limited amounts and mainly for selected export transactions at present.

Deposits are estimated at FG 3 to 4 billion (over half of the new currency issued in exchange for sylis at Conakry exchange points in January, 1986) and are growing, even though the banks do not yet offer interest-bearing deposits and require minimum deposits of GF 100.000 (equivalent to one year's official salary for many civil servants). At least two of the banks, BIAG and BICIGUI, appear to have substantial liquidity, followed by SGBG, which in fact appeared to be short of funds and seeking to borrow from the Central Bank. The ongoing liquidation of deposits on record at the state banks, estimated at GF 11 billion, of which perhaps GF 7 billion are owed to the private sector, should also contribute to the growth of their deposit bases as these accounts are settled and the funds paid out during the next few months. Finally, BICIGUI expects that the new branches it is committed to establishing in major towns in the interior will generate deposits steadily, if only for security reasons (as in Conakry at present).

The banks also hold some foreign exchange accounts which Guineans are currently allowed to open. Reportedly BIAG holds some two-thirds of these funds, with most of the balance held with BICIGUI. Although external funding lines should be available in theory through the banks' shareholder networks, these are not yet in use, since cash collateral is currently required for import transactions.

It is therefore reasonable to conclude that the banks will have little difficulty generating loanable funds, although it is impossible to even roughly guess at the future rate of deposit growth and its significance in relation to the demand for and supply of credit. This judgement is reinforced by the additional considerations summarized below.

- If the full GF 20 billion has been absorbed by the interior and the full GF 7 billion of estimated frozen deposits were to be paid out (taken only as assumptions), the current demand deposit base of up to GF 4 billion would represent only 13 percent of private sector liquidity. This is an extremely low rate compared to neighbouring countries--even Mali's money supply had a deposit to currency in circulation ratio of one to three in 1982, which grew rapidly to over one to one in 1984 when it joined UMOA.

- A basic, steady increase in confidence in the banking system and the opening of BICIGUI branches in key towns should raise the deposit rate to one at least roughly comparable level to that of Mali prior to its drive to enter UMOA. If Guinea also were to join UMOA or otherwise achieve convertibility for its currency in the next few years, this would also increase the deposit rate, since it would bring confidence in the stronger currency and some repatriation of CFA accounts.

- The Central Bank is bound to begin offering discount facilities, which are a major potential source of funding for commercial banks and directly tied to credit operations.

- Finally, the introduction of interest-bearing term deposits should help improve the maturity structure of these liabilities, especially if no interest is required on demand deposits. This is a policy now followed in the UMOA and (UMCA??) countries, which is proving to be effective in increasing the volume and market share of term deposits.

(iii) Current constraints on bank lending

Despite the successful start-up of the three principal commercial banks, there are a number of factors which, taken as a whole, appear to be restricting the banks in carrying out their intended (i.e. largely short-term trade- or working capital-related) lending activities:

o Infancy of the banks

The banks point out that they have not been in business long enough or had enough contact or experience yet with (potential) borrowers to engage in anything buth "trial" lending on a very small scale (BICIGUI and SGBG only started up in January, 1986, and BIAG in August, 1985). In any case, no matter how high one's expectations, it is difficult to judge what would be a reasonable "settling in and familiarization period" for a new bank in Guinea. Certainly the near-total absence of a private sector credit market until (potentially) now, coupled with more "technical" constraints, makes this a particularly challenging environment in which to begin operations. The anticipated currency conversion and, to a lesser extent, the devaluation were additional factors affecting BIAG's willingness to engage in lending in its first five months of operation prior to this policy action.

o Attraction of other income generating activities

The banks are providing already a range of services for which they are charging substantial fees, which reflect the high cost of doing business in Guinea but also include a significant element of profit. These include currency exchange, overseas draft collection, payment transfers and some documentary credits. The services are so expensive and the delays caused by Guinea's infrastructural isolation from the rest of the world so substantial (part of the reason for the high cost) that clients with large transactions have found it more economical already to fly to the foreign bank's location than to use the local bank's services. However, fee-generating business appears to be brisk at all three of the principal commercial banks. Taken together with their present pre-occupation with developing operating systems and training staff, the volume and profitability of this type of service will continue to compete with the development of loan portfolios.

In addition, once the Central Bank begins to pay interest on commercial bank deposits (over and above required reserves), and an interbank market begins to develop, the banks may tend to place their liquidity within this system, which would also have a dampening effect on the development of a domestic credit market. An interbank rate (i.e. taken here to mean the rate offered not only by the banks to each other, but also by the Central Bank to the banks, as in the UMOA countries) slightly higher (e.g. by one percentage point) than that practiced by BCEAO (West African Central Bank) branches in the UMOA system is being talked about as a potential interbank rate in Guinea. The intent of this policy would be to discourage capital flight and to maintain the value of the Guinean Franc. The BCEAO rate is currently 10% and changes infrequently. Since it is quite favorable under current maket conditions, banks in UMOA countries do tend to seek this interest income at the expense of lending. In addition, the Central Bank may not discourage this practice, in its desire to control liquidity and potential inflation.

Finally, trade financing and other off-balance sheet transactions (such as loan guarantees) are likely to become a major activity of the banks, based on external funding lines made available by foreign shareholders and perhaps tied initially to prior export transactions.

- Absence of a national credit policy

The Central Bank (BCRG) was authorized to lead the formulation and enforcement of a national credit policy in its new charter, which was issued in September, 1985 and accompanied by a decree announcing its new organizational structure. The BCRG has not formulated a credit policy as yet, but officials interviewed hoped that most elements of such a policy would be in place within three or four months. It is still pre-occupied with developing its own internal systems, liquidating the state banks, and firming its grasp on activities already undertaken, such as the administration of the weekly foreign exchange auctions and the import regulations which it established in January. The BCRG is also awaiting the tabulation of the amounts of new currency made available for exchange for the syli in the interior of the country.

The BCRG is still in its formative stages as an organization and has no firm idea yet of the country's overall money supply situation. The latter problem at least should be resolved soon and in any case would not necessarily impede its development of a basic framework for the regulation of credit. In fact, the delay in announcing such a framework and a more specific timetable for its effective establishment is becoming more of an issue as time goes on, suggesting that the BCRG is having difficulty organizing itself as quickly as might have been hoped.

The future credit policy could involve the following regulatory restrictions and requirements, including features found in the UMOA system or UMCA (Central Africa) systems:

- credit ceilings (e.g. on total credit to the economy, on individual bank portfolios and leverage ratios, on individual borrowers);

- sectoral lending requirements (e.g. by business activity or size of the borrower);
- other controls on the composition of loan portfolios (e.g. by maturity structure);
- liquidity requirements, including statutory and other reserve requirements;
- an interest rate structure, (e.g. Central Bank discount rates, floors and/or ceilings on bank lending rates).

The absence of <u>all</u> of these credit policy instruments has the following major <u>consequences</u> which do constrain commercial bank lending, if only temporarily.

- The Central Bank is not paying interest on commercial bank deposits, as does the BCEAO, which significantly contributes to the liquidity of its branches and therefore to their discounting activities.
- The banks cannot transfer credit risk yet to the BCRG by rediscounting loans: liquidity and organizational concerns might be among the principal factors delaying this development. Until government local currency deposits (based for example on the sale of securities and a genuine tax base) are generated, Central Bank liquidity will be based largely on commercial bank deposits with it (not yet established), donor counterpart funds (thus far difficult to access and use), and other sources not based on public revenues.
- No interbank market has as yet been established; although commercial banks in Mali, for example, are not significant borrowers on this market, they have been substantial depositors with the Central Bank and the national development bank. In Guinea, where the potential deposit base is still restricted due to (hopefully) short-term circumstances, an interbank market would at present add some flexibility to potential credit decisions. For example, it appears that SGBG would have borrowed already on such a market: according to one source, BICIGUI has captured an estimated 2/3 of local currency deposits, with BIAG in second and SGBG in third position.
- No interest rate structure has been developed yet for loans or deposits. If UMCA practiced were mirrored,

the Central Bank would announce sets of preferential and ordinary rates at which it would discount notes and banks would be allowed to lend, a deposit rate for funds placed with it and rates for various types of deposits held by the commercial banks. Anticipation that a rate structure will be announced relatively soon does have a dampening effect on credit activities in such a new environment.

It is important to note that this absence of a credit policy system and Central Bank rediscounting does not equate to a prohibition of routine commercial bank lending activities. In fact, the banks are free to charge the interest and fees which the market will bear. It is futile and premature to criticize the banks for not having extended any substantial credit by now (given the other constraints and the small overall local currency deposit base, equivalent to about $10 million). However, there is no reason to believe that the policies and services which the BCRG will be establishing will differ in any critical respect from those in effect in UMOA member states, at least insofar as the differences would invalidate or render unprofitable loans extended prior to their implementation. The banks' managing shareholders are used to operating within the type of framework which is likely to be put into place soon and could therefore proceed within reason. Nevertheless, the lack of interest rate and other credit guidelines, discounting facilities and the like do result in an environment which does little to support the development of a credit market at this time.

o <u>Absence of an adequate legal framework for the creation of liens and other binding obligations</u>

There are hardly any appropriate legal mechanisms or instruments for establishing collateral control over borrowers' assets and contractual obligations with well-identified entities; e.g. no property law or title registration system, no mortgage and lien creation and registration system, no confidence in the vehicle registration system, no associations law and an imperfect company and commercial law, etc. Some of these deficiencies can be resolved readily by the adoption of new legislation, but even they will need some time to be mastered and administered as intended by the relevant authorities. Other problems, such as the lack of a land title registration system, require time-consuming preparations (e.g. cadastral surveys). While the banks and their clients are beginning to improvise already in some of these areas, they are not relying solely on ad hoc, legally groundless or incomplete formalities to protect their interests, and thus being nearly as cautious as the absence of these legal structures would warrant.

d. Prospects for rural sector credit

As has been seen, present access to domestic credit by pr entrepreneurs is severely limited, except for those wh participants in the "supplier's credit system". Even whe commercial banks are in a position to play their role freely and actively, which should be by the end of the s or the beginning of the third quarter of this year, the sector, including all segments of the private sector ou of Conakry, will by and large have no direct access to c facilities in the near future, except in pockets specific development projects operate, in towns where branches are to be established, and in exceptionally s cases (e.g. a prominent trader in Kankan who maintains ba relationships in Conakry).

At the moment, there are no banks at all outside Conakr two of the three banks have no plans to establish bra up-country for the time being. In addition, BIC branches in major regional towns will only provide partial coverage of the rural sector. Although these br have the potential of generating solid local deposit they will not necessarily be active lenders to the private sector in the short term. For example, if the b demand comes from a multitude of applications for small from small enterprises inexperienced with commercial credit requirements and practices (which is en possible), the administrative burden and cost of ser this demand would be quite high, as would the perceived involved.

However, if the credit risk itself can be passed on t discounting to the BCRG or avoided through the managem donor-supplied funds (as in the structure recommended for the proposed USAID program), branches of BICIC ultimately the other banks (presumably headed by one c expatriates) should be capable of managing the extens credit to local businesses and associations, and willing so for appropriate fees.

3. Private Sector Demand for Credit

a. Farmers

The volume of demand for credit by farmers correspo their financing needs for the purchase of equipment and such as fertilizer, pesticides, tools and spare parts, purchase of construction materials for housing, stora irrigation or drainage, and for bridging periods harvests. Taken individually, these demands are not bankable because of their small volume, lack of coll and their high level of administrative expense.

Due to the absence of adequate producer prices, and the Government's lending focus on the public/parastatal sector, the (potential) demand for credit from private farmers has not manifested itself for twenty years. In addition, a history of collectivization, forced mobilization of production and discouragement of private marketing has resulted in a considerable loss of confidence in government organizations, including would-be extension agencies or rural commercial entreprises and the banking system itself, which was Government-owned until a few months ago.

Now that indicated government producer prices have been increased for certain key commodities to reflect market conditions, and free private trading (at free prices) is being encouraged for all produce, one can expect farmers to start increasing their production with an accompanying increase in demand for various kinds of inputs. As an example, the IBRD Agricultural Sector Review (GUI-4672 of 04-15-84) reported that projections indicate that demand for fertilizer could well exceed 50,000 tons per annum by 1990, which would be a tremendous increase compared with the three to five thousand tons per annum imported during the last few years. However, it is generally agreed that the majority of farmers cultivate in a rather basic and unsophisticated manner--there have been no extension services for two decades--and that their aggregate demand for inputs is likely to be much more modest initially.

The demand for construction materials has been quite visible in the past two years in the rural areas. For example the regional state stores which have now been closed (the ERCOAs) reportedly had an unusually successful coffee collection season in 1984-85, when they began offering cement directly against the product, rather than selling it at a subsidized rate independently from cash payments for the crop (at the formerly derisory official producer price). The liabilities left behind by the ERCOAs in fact will be difficult to liquidate, since in certain regions they are expressed as in-kind debts of cement and other materials. However, it is not clear that the demand which emerged pursuant to this practice is at the farm level. For one, the ERCOAs used local merchants as intermediaries in the coffee region in 1984-85: in many cases they bought the coffee for cash from the farmers and accepted cement from the ERCOAs for resale in town. Also, although some of the purchasers of coffee in this first "open" season continue to offer cement for produce, farmers are reportedly demanding cash now in view of the fourfold increase in the indicated producer price. It is hoped that, apart from the development projects, farmers' demand for various supplies will be met by traders willing to extend credit. However, this could involve fairly complicated transactions, for example quasi-barter arrangements involving a lien on or purchase agreement for the season's output, and would involve a production risk which merchants (and banks) might not be willing to provide, particularly to small farmers or unproven new rural associations.

b. Traders

The trading community requires credit to finance the importation, storage and distribution of consumer and other goods, and is the segment most likely to rapidly absorb available credit, particularly since leading merchants are the strongest group of would-be Guinean borrowers, financially and in terms of business experience. Returning expatriate Guineans may also begin establishing themselves through trade, if anything to generate a local currency base (as in the case of former PLC group members). Their demand for credit will also grow with their desire to diversify into other activities (e.g. transport and manufacturing). As indicated earlier, traders have been relatively successful, through suppliers credits and offshore accounts and cash collateral, to obtain finance and foreign currency when it was not officially available. With the new banking system and the foreign exchange auction, the traders are likely to gradually avail themselves of these formal sector services.

In the short term, however, many traders and other classes of borrowers will remain suspicious of banks, particularly as long as their deposits in the defunct state banks have not been repaid to them. Under these circumstances, it is more difficult than usual for good working relationships to be established between banks and their clients. Many may prefer to borrow from the supplier's credit system or other traditional sources for the time being.

For their part, the banks will have to qualify their clients for the first time, in most cases without the benefit of written records of the applicant's prior business activity, credit history and current financial condition. The process of developing this type of information might seem like an intrusion to some would be borrowers, or play up their lack of experience, which will deter the banks.

c. Transporters

Another source of potential demand for credit related to the rural sector is road transport, which provides the vital link between Conakry and the regions and is an equally dynamic sector in the current liberalized environment. Transporters were the second most active group of entrepreneurs under the previous regime and have therefore also generated savings and are likely to require and occasionally qualify for credit. The country's commercial vehicle fleet is generally in bad shape and in need of renewal, but both small and large transporters are thriving on the steady increase in demand and the effective deregulation of prices, to the point of being accused of exploiting the public on the excuse of the recent increase in fuel prices. New commercial vehicles are in evidence, typically purchased in Nigeria, Liberia and other West African countries with externally-held funds. While most transporters are capable of covering their current level of operating expenses, including affording spare parts, the availability of the latter as well as tires, fuel, etc., now a significant problem for them, could be improved if credit were extended to suppliers of these goods, including (potentially) to transporters' groups created for that purpose.

Transporters have been among the most active applicants for loans under the World Bank's small enterprise loan program, of which 25% had at one point been set aside theoretically (if anything as an upper limit) for truck financing. In recognition of this demand, a new transport sector credit program which the World Bank is preparing may provide for the financing of an additional 250 trucks to the private sector. Unfortunately, the experience which might have been gained by now with the truck financing applications on file and approved under the small enterprise credit program has not come to pass, due to the massive currency devaluation in January. Since the program requires a local currency downpayment of 40% (a requirement which reportedly could be relaxed soon to ease the bottleneck), contributions which seemed reasonable when calculated on the basis of the former exchange rate (e.g. 3-400,000 sylis for a one million syli vehicle) are now beyond reach for the applicants (e.g. 3 to 4 million GF for a nine million GF transaction, including freight, insurance and duty now calculated on the basis of the real exchange rate).

d. Small service and industrial enterprises

Demand for credit will also be generated by the financial needs of small and medium sized enterprises associated with the rural sector, i.e. repair shops, assemblers or manufacturers of agricultural equipment, tools and inputs, etc. This source of credit demand is easier to spot, since it has prompted numerous applications to the Ministry for Small and Medium Enterprises, which had been managing a World Bank credit line (until recently) since 1980-81 and received private sector medium and long term credit applications totalling about US $30 million in foreign exchange. That was the first indication of potential demand for credit in support of investment by the private sector, and it included a good number of project proposals in the agro-processing and agro-industrial field (e.g. a manufacturer agricultural tools, feed and flour mills). The World Bank line has been moved from this agency and the National Bank for Commerce, Industrie and Housing (CNICH) to BICIGUI, since CNICH has been closed down and the agency reintegrated into the Ministry of Industry and its status made pending. Approximately $200,000 of the $9 million budgeted since the beginning has so far been committed, although not yet disbursed. As mentioned above, activity under this credit program has practically come to a standstill since the devaluation of the Guinean currency, which led to a 15-fold increase in the amount required from project sponsors as local currency investment.

e. Conclusions

The two principal conclusions to be drawn from our research are that:

- the potential demand for credit has not been and probably cannot be meaningfully quantified at present; and
- the potential demand for credit is certain to far outstrip the prospective supply of credit in the years to come, making this a high priority sector for donor assistance.

(i) Quantification problem

With the exception of the loan applications mentioned before, no figures or other information are available on which to estimate (potential) credit demand in Guinea at present.

Smallholder farmers, and the private rural sector in general, have been severely neglected for twenty years. They have been deprived of productive inputs, extension services and credit to the point where no one really is in a position to quantify what it will take to redress the situation.

The private commercial sector has had to hide in the shadows of the "parallel market", but has survived by doing so and by using traditional supplier's credit systems. It is now emerging again and showing signs of vitality, but it remains to be seen what its capabilities and requirements will be as it re-enters the formal economy. This applies equally to the private transport sector.

Although applications for medium/long term loans from other types of small enterprises give some indication of possible demand, actual commitments and disbursements so far have been very small indeed and the amounts applied for cannot be relied upon to reflect effective demand for that type of credit.

All three new commercial banks acknowledge that they were not able to undertake any market or credit survey before setting up business. They believe that sufficient lending opportunities will gradually develop, but without being able to quantify them to any meaningful extent at this point in time.

The Central Bank also confirmed that the situation is very unclear and that it is unable to give estimates of aggregate demand for credit, let alone broken-down projections for specific parts of the private sector.

Finally, the consultants working with IBRD and the Central Bank on the liquidation of the state banks echoed the uncertainty and ignorance related to (potential) demand for credit expressed by others, as did the officials involved in the supervision of credit lines provided or to be provided by the World Bank, the European Development Fund and the Caisse Centrale de Cooperation Economique.

(ii) Prospective demand for credit

Although our attempt to determine and quantify current demand for domestic credit, and the anticipated demand for the next 2-3 years, has not produced a measurable result, there is ample justification for pursuing the proposed USAID credit program.

When one considers that the private sector, especially in the rural areas, has been the victim of adverse Government policies and neglect over a protracted period of time, one has to conclude that a great deal of rehabilitation and re-development is called for.

When one also considers that large parts of the parastatal sector have been or will be closed down, and that it is intended that the private sector takes over or replaces many of those activities, it is clear that a great deal of additional re-development and new development is to be carried out as well.

There is no doubt that the country needs all the resources available, and more, to reform and reconstruct its economy. The proposed USAID grant is a key resource in that context and at this point in time, and we believe that the credits it can generate will respond to very real demand even if that is not quantifiable at present. How that can be achieved is the subject of the following sections.

B. IMPACT OF DONOR PROGRAMS ON CREDIT AVAILABILITY AND TI POTENTIAL ROLE OF THE PROPOSED USAID PROGRAM

Before assessing the impact of donor programs and that o: proposed USAID program on credit availability, it shoul pointed out that it is the effect on credit to the pr sector that is of concern in this exercize. The analys: therefore confined to a discussion of donor programs directly involve the extension of credit to the pr sector. However, other types of programs should hav impact on credit availability. For example:

- Donor funding for the rehabilitation of state enterprises to be maintained as such (e.g. su(the utilities) will lessen pressure which othe might develop to service their needs (even if were discountable with the Central Bank and ther hardly to impose risk on the banks).

- Technical assistance in a variety of areas, su in the creation or improvement of legislation a the development of a macro-economic plannin(management system, will improve the ba environment little by little.

The discussion below summarizes donor activity, or note lack thereof, in the extension of five types of finance:

- Foreign currency credit and local currency cred:
- short-term credit (up to 1 year) and medium to long-term credit (1 to 10 years); and
- equity finance.

1. Impact of Donor Programs on Credit Availability

a. Foreign currency credit--short term

A certain amount of this type of credit is or wi available from donor programs, particularly throug: agricultural development projects mentioned previously loans will be repaid in local currency. Since projects o nature include extension services and are managed/supe by professional personnel, they should result in an eff application of the available credit and have a reasonabl of success in obtaining repayments. In addition, r achieved and experience gained in these projects will value to similar projects in the future.

However, such projects only cover specific geographical and have a long gestation period, both of which limit impact.

Another potential form of short-term foreign currency credit is that offered by foreign suppliers. At present, the Central Bank requires that the full amount of foreign exchange bid for on the basis of import licenses be covered in local currency by the importers. However, there is every indication that this requirement will be lifted in mid-1986 to allow importers to whom suppliers are offering credit to deposit local currency only as the foreign exchange is disbursed pursuant to the terms offered by the suppliers. However, access to this type of credit would be limited typically only to importers who are well enough established in the eyes of foreign suppliers.

Thus, there is a <u>very considerable gap in the availability of short-term foreign currency credit, particularly to the rural sector and smaller businessmen</u>.

b. <u>Foreign currency credit--medium and long term</u>

A good deal of credit of this type is and will be available from credit lines (being) established by several donors. The programs currently in effect or soon to be finalized are described below.

- <u>World Bank line of originally US $9 million which has been in place since 1980</u>.

As noted earlier, commitments and disbursements have been disappointing. However, now that the line is lodged with and handled by a professionally-run bank (BICIGUI), <u>assisted by a CIDA-seconded development finance expert</u>, and following the devaluation of the currency and the liberalization of the economy, effective demand for this type of credit should increasingly manifest itself. Loans under this facility are for rehabilitating existing or establishing new small and medium-sized enterprises that are involved in industrial, agro-industrial or agricultural activities. The loans are typically aimed at financing the acquisition of machinery, equipment, etc., not locally produced or available. Experience so far has indicated that most Guinean entrepreneurs have not had the opportunity to acquire experience with sophisticated or large-scale manufacturing or processing plant, and it is anticipated that the maximum size of projects financed under this line will be around US $500,000 for the time being. Borrowing terms are relatively stringent in that the foreign exchange risk lies with the project and interest amounts to 13% p.a.

The interest paid by the borrower is shared by the financial institutions involved: 3% remains with BICIGUI as a management/administration fee, while 10% is paid to the Government, (in a special central bank account). Apart from forming a local currency fund which is to be converted when re-payment to is due to the World Bank, the 10% so reserved also acts as a buffer to provide against default by project borrowers. The credit risk, therefore, lies with the government, and not with the commercial bank.

- <u>European Development Fund (FED or EDF) line of credit (ECU 4.1 million)</u>.

The purposes and mechanics of this line are very similar to that of the World Bank project. The EDF line is also lodged with and handled by BICIGUI, <u>assisted by an EDF-seconded development finance expert</u>. Borrowing terms are softer, and the credit is aimed at smaller enterprises with a maximum loan amount of ECU 50,000 for the time being. The interest rate is 8 percent (3 percent for BICIGUI and 5 percent for the Government) and the exchange risk is for the account of the government. The credit risk is also borne by the government. Official ratification of this credit line is expected very soon.

- <u>CCCE credit line, denominated in French Francs (30-45 million).</u>

Details of this proposed line are being worked out at present, and it is hoped to put it in place in three to four months time. Although the general objectives, conditions and mechanics of this credit line are very similar to those of IBRD and EDF, there are a few interesting differences. Firstly, the credit will be available through all three commercial banks, and not only through BICIGUI. Secondly, the Caisse has insisted that the banks carry 20% of the credit risk, in return for which they will receive an extra 2% interest margin on top of the 3% for management and administration. The banks will nevertheless be <u>assisted by development finance experts seconded by CCCE</u> who, like those seconded to BICIGUI under the IBRD and EDF lines, will be based in Conakry. Interest to the borrower will be 10%, of which the government received 5%. The government will also carry the exchange risk, and 80% of the credit risk.

It appears that <u>these three specific donor lines provide an adequate supply of foreign currency-denominated medium and long term credit</u> at present. The funds will be managed professionally and made available only to projects that have undergone a thorough economic and financial evaluation. The lines are available for projects <u>throughout the country</u> and, in view of the anticipated low initial absorption capacity, <u>should not suffer from any serious gap in timing</u>.

There are other donor programs under consideration which are also likely to provide this type of credit, such as the World Bank transport sector credit which reportedly includes a provision for financing 250 trucks for the private sector, and UNDP's investigation of mechanisms to lend to cooperatives, savings associations and other rural organizations once they have been established as legal entities.

c. Local currency credit--short-term

By definition, no donor is in a position to lend or grant local currency as such. There are, however, a variety of donor programs which generate local currency-denominated counterpart funds. They are usually invested on a medium/long term basis in government-budgeted projects, and are not normally available to the private sector as short-term credit.

The private sector is, therefore, dependent upon the commercial banks for short-term domestic credit and, in Guinea, also on the "informal" supplier's credit system described earlier.

As mentioned elsewhere, the commercial banks, guided by the Central Bank, are currently very cautious in beginning their lending activity. Once a credit policy has been established by the Central Bank (particularly an interest rate structure and a discounting mechanism), the commercial banks are likely to expand lending. The extent to which bank credit will grow is difficult to estimate and will depend on a number of factors (as in the constraints enumerated earlier). In the very short term, funding could constitute a problem. The timing and the amount of frozen deposits that will be returned to the private sector by the defunct state banks, and how much of that will be re-deposited with the commercial banks, could be a major factor in determining short-term funding ability, as would prolonged delays at the Central Bank in setting up the discount mechanism.

Although the closure of a number of parastatals will reduce credit demand from a sector which previously absorbed 95% of all domestic credit, the privatization or other restructuring of some parastatals might create priority credit needs to get the more viable firms back on their feet, thus renewing their competition for credit with the private sector. At present, parastatals are being funded and their liquidity managed outside of the commercial banking system (e.g. they were issued 3 billion GF at the time of the currency conversion in January and operate under strictly-defined budgets). Reportedly, once these enterprises are re-integrated into the market, BICIGUI might be asked to play an early role as their lead banker.

Recourse to "traditional" supplier's credit will continue to be an important source of local currency credit, particularly given the lingering mistrust of banks, the nature of old established relationships and vested interests, and the absence of a rural banking network. To what extent the "traditional" systems of credit will play a role and for how long is hard to say. Parts may merge gradually into the banking system as its financial intermediation role develops, and other parts may dry up. It is very likely that this "traditional" system can no longer play the same role as it did before, if only because the private sector is now largely free to pursue its own interests, and its demands and requirements are, therefore, likely to outstrip the "traditional" system's ability and capacity to service them.

Overall, it seems probable that local currency short-term credit will be in short supply for most of the remainder of 1986 and thereafter, from time to time, in sympathy with seasonal variations in economic activity.

d. Local currency credit--medium/long term

The local currency denominated counterpart funds generated by several donor programs are either grant funds or repayable typically over extended periods of time and, therefore, they provide a suitable source of medium/long term credit. However, most if not all of these funds have been or will be committed to various government programs/projects, and little if any is aimed directly at the private sector.

In the absence of any local development finance institutions, and with the commercial banks being unable to lend medium/long term in view of the short maturity profile of their deposit base, there appears to be a very considerable shortage of this type of credit. This does not manifest itself in any dramatic way at present (given the latency of credit demand), but it will not be long before the private sector will be looking and asking for medium/long term local currency credit in significant amounts. There will be the requirement to rehabilitate and build new warehouse and storage facilities, factory and workshop buildings, as well as other local currency investment needs that cannot appropriately be financed by short term credit, even if that were adequately availabl.

e. Equity Finance

Finally, there is a growing need for equity capital to complement loan finance and to act as the prime bearer of entrepreneurial risk. No donor programs generate or provide any finance of this type, nor is their any Guinean institution that does. This type of money would normally come entirely from the local private sector, except where foreign joint venture partners put up some of it. The Guinean private sector in most cases will be unable to provide sufficient equity capital to meet (reasonable) requirements in this

respect from both foreign and local
or finance is, therefore, bound to
block in the development of the p
Guinea.

2. Potential Role of the Proposed US

As discussed in detail in Section (
to offer local currency credit throu
system, preferably to enterprises
dependent upon rural marketing and
The funding from this program will
$10 million in hard currency into t
offered as a grant to the government

The proposed grant will be a major
private sector as soon as it is an
renew and consolidate confidence in
will play a key role in its use. It
for the government to continue the
reform and liberalization measures
consider additional policy changes
be useful or desirable.

More specifically, the grant will h
access to credit, demand for cr
credit. The preceding analyses show

- most private entrepreneurs
  the rural sector has virt
  bank credit facilities;

- meaningful quantification (
  possible at the moment, b
  development needs of
  privatization and re-dev
  economic sectors leave no
  for credit must exist;

- there is a serious short
  currency credit for the co
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  involved;

- there is a current shortag
  currency credit for the co

- there is a considerable sh
  local currency credit for
  and

- there is a serious shortag

<u>Access</u> to credit for the commercial and rural sectors will be created by putting the grant funds at the disposal of the commercial banks, both as hard currency for imports in the first phase (assuming, as we recommend, that the foreign exchange is not sold through the auction), and in local currency for various uses (including possibly for foreign exchange purchases if permitted) in the second phase of the program. With the credit in the first phase, the borrowers will be in a better position to distribute imported goods to the rural sector, as well as the credit which finances them. The local currency loans can be put to a very wide variety of uses mentioned elsewhere.

Although the effective <u>demand for credit</u> is an unknown quantity at this point, the proposed US $10 million is a very considerable amount in the context of Guinea's economy today (roughly equal to total bank deposits at the current exchange rate) and should go a long way in meeting immediate requirements for inputs and consumer goods.

The increased <u>availability of credit</u> which will be a direct result of the grant, appears to be a useful complement to other donor programs, none of which provide short-term credit in any form or medium/long term local currency credit.

Focusing the program as much as possible on rural marketing and distribution will make it an excellent complement to other donor programs (in addition to unrelated uses of the credit), some of which are discussed in Part II, such as:

- restructuring and/or liquidation plans for the Ministry of Rural Development, SEMAPE (agricultural inputs parastatal), AGRIMA (agricultural equipment), PROSECO and FRUITEX (both in commodity exports);

- current liquidations of the truck fleets, warehouses, and inventories of the ERCOAs (43 regional state stores), ALIMAG and ALIDI (Conakry state stores), the potential liquidation of COTRA (rural trucking) and COTAX (rural taxis), and the attempt to privatize the distribution of fuel, currently managed by ONAH;

- agricultural development projects with or without credit components, as well as agro-industrial investments which might be contemplated and which donors might support;

- UNDP efforts just underway to design an accounting plan and otherwise assist in the development of rural savings associations, and the research of other agencies, such as FAO, into rural credit issues;

- the donor hard currency credit lines mentioned above.

The USAID program will create ... ly source of funding for these and strictly private ini... ...es which have a direct or indirect impact on rural marketing and distribution. With the appropriate management and technical support, it can experiment with and spur private efforts in a field which might see little active support for an extended period. The program will also provide a testing ground and reference point for the policy and planning efforts undertaken in many other areas.

C. DESIGN CONSIDERATIONS AND TECHNICAL ASSISTANCE REQUIREMENTS FOR THE PROPOSED USAID PROGRAM

The initial design concept for the proposed USAID program, as stated in the terms of reference and other working documents, can be summarized as follows:

- USAID would make $10 million available as a grant to the Central Bank, which will be disbursed to it in two tranches and will generate local currency counterpart funds. This step is referred to hereafter as "Phase I" of the program, or the "grant".

- The counterpart funds would then form the basis for a local currency credit program, intended to be administered by the commercial banks and hopefully to be directed to enterprises involved in rural marketing and distribution activities. This will be referred to as "Phase II" of the program, or the "credit program".

1. Phase I Analysis

It was assumed at the beginning of the design effort that the hard currency grant would be disbursed through the auction system. The objectives of this sale can be stated as follows:

- to support private sector importing by adding non-tied resources (to source of origin or type of product) to the pool of available foreign exchange;

- to minimize the need for USAID supervision at this early stage; and

- to build up the counterpart fund as quickly as possible (i.e. assuming that the auction were working properly).

In other words, any positive impact of Phase I on rural marketing and distribution activities would be incidental at this stage, the objective being to generate loanable funds quickly. For example, a question for consideration was whether or not it would be desirable to experiment with demand for agricultural input (or perhaps spare part) imports by tying a small portion of the foreign exchange sale to import authorizations for this category of products. Although this action would test demand, it was feared that it might slow the disbursement of the funds and complicate the administration of the program.

As our investigation proceeded, it became apparent that an alternative mechanism might be more effective in achieving a rapid disbursement of the hard currency funds and furthermore could have a more direct relationship to the key objectives of the Phase II local currency credit program than would a sale through the auction. This mechanism would provide for the short-term lending of the foreign exchange (repayable in local currency) to importers (at the prevailing auction rate). Under present circumstances, we recommend that USAID adopt this approach for Phase I, on the basis of the analysis presented below.

Auction

Credit

-Collection

Before discussing the merits of a Phase I hard currency credit program relative to an auction sale, however, it is appropriate to point out that the speed at which the counterpart fund is built up is not assumed to be a key issue in the discussion, and may in fact be academic. This concern could be substantially alleviated or completely eliminated if the build-up of the counterpart fund were dissociated from the rate of disbursement of the foreign exchange grant. It is entirely conceivable that the Guinean government would be willing to create advance local currency to the counterpart fund account from reserves immediately upon the transfer of the grant funds to the Central Bank (i.e. in two tranches as envisaged), or at least in accordance with an agreed-upon schedule which is unrelated to progress in the disbursement and repayment of the grant-based hard currency loans.

We highly recommend that such an agreement be sought from the government, since it would permit Phase II local currency lending to begin at a definite (and earlier) point in time. This approach would probably be taken as a matter of course if the hard currency were to be sold through the auction, since the USAID funds would be commingled with other sources of foreign exchange for the auction (i.e. government and donor resources). Local currency would necessarily have to be paid into the counterpart fund account according to a schedule, if anything based at a pace which roughly approximates that of the sale of USAID-supplied funds as a proportion of other sources of hard currency for the auction, since it is unlikely and certainly not necessary that they be accounted for separately once they have been transferred to the Central Bank.

Good

Although this would not be the case under the proposed Phase I hard currency credit approach, where the funds would be specifically identified as a credit line, it is still difficult to imagine what might be a reasonable objection to an immediate or at least an independently scheduled pay-in rate to the counterpart fund account. In particular, we do not believe that the lack of local currency liquidity at the Central Bank could be advanced as an argument against dissociating the counterpart fund build-up from the performance of the Phase I credit program. Although a credit risk would be involved, this risk could be borne by the counterpart fund account itself, from which losses could be deducted.

a. Rationale for the proposed Phase I credit program

USAID's desire to help with Guinea's balance-of-payments and to support private importers in Phase I can be achieved both through the proposed credit program and through the auction at a reasonably fast pace. Demand for the funds will be greater under the credit approach, but it may take additional time to qualify borrowers. Although there have been problems with the auction, the two tranches of $4-5 million represent at most two months of projected disbursements through this system. However, if the auction were to bve discontinued or the market's absorptive capacity diminished in absolute terms or dwarfed by proposed contributions to the auction, the credit program would clearly result in a more rapid and predictable disbursement rate.

The key factor behind our recommendation is the fact that the central goal of the government is to encourage foreign exchange transactions and trade to pass through the official system, as well as to generally promote recourse to the new financial sector. Although the opportunity to purchase foreign exchange would normnally be welcomed, the business community has been slow to participate in the auction, for reasons stated below. Presumably the traders, particularly the smaller ones, who continue to import goods as before still rely on foreign exchange held outside of the country, purchased on the parallel market, or acquired through proceeds of export sales within the region (gold, diamonds). Under present circumstances, the objective of encouraging recourse to the banking system can best be reached by disbursing the hard currency grant through a BCRG credit line which the commercial banks would access on behalf of importer clients, with the credit risk to be borne by the Central Bank.

The foreign exchange auction functions roughly as follows:

- o an import authorization is obtained from the relevant authorities (now the Central Bank);

- the prospective importer submits his bid for foreign exchange to his commercial bank (specifying amount and price), accompanied by the import authorization;

- the Central Bank reviews all of the bids, determines the weekly exchange rate and allocates the budgeted weekly amount of foreign exchange among successful bidders (define), against a transfer of local currency to its accounts which fully cover these allocations.

Trading volume was as follows during the first seven auctions:

- a total of $1.2 million during the first four auctions (up to February 14)

- a total of $3.2 million during the next three auctions (up to March 7)

The auction rate has fluctuated between 340 and 370 Guinean francs to one U.S. dollar. State enterprises and the large mining companies do not use the auction, and in fact the latter indirectly are major contributors to it. In addition, importers of six essential commodities (rice, flour, sugar, milk powder, tomato paste and cooking oil) temporarily are permitted to purchase foreign exchange at the rate of 300 FG to the dollar.

Projected rates of disbursement for the initial period were considerably higher than results: $1.0 million per week for a total of $10 million by March 7. As noted by USAID, the target was not reached because of:

- delays in starting the auction in early January as planned;

- uncertainty over who is eligible to participate in the auction (e.g. the Lebanese community in particular);

- the lack of confidence of some importers in the system and the ability of the parallel market or external accounts to meet their present needs; and

- the lack of liquidity of some importers which prevented them from purchasing the foreign exchange at 100% cash terms required, or to otherwise engage in significant transactions;

In addition, demand for foreign exchange was arguably limited by continued recourse to other sources of foreign exchange and by donor funding (e.g. the CCCE credit for the Societe Generale de Commerce, various commodity assistance programs such as PL-480) for basic food commodity imports retailed by local traders. The latter factor effectively removes local currency from the potential pool available to buy foreign exchange through the auction, by tying it up in purchases of high volume, fast-moving products from the donors or SGC.

We concur in USAID's analysis that the recent increase in demand for auction funds was caused by the following:

- increased pressure placed by the Central Bank and the IMF on the commercial banks to promote use of the auction among leading traders;

- the fact that banks have begun to extend credit to some of their clients to help them meet the 100% cash terms of the auction;

- the further streamlining of the import authorization process, now managed entirely by the Central Bank.

Although discussion are in progress as to means by which to improve the functionning of the auction, disbursing the hard currency grant through a credit line clearly would avoid the two fundamental problems facing the auction system as it is presently conceived.

- Liquidity problem

The lack of local currency liquidity of prospective importers restricts their ability to bid for foreign exchange in the auction, which requires that bids be 100% covered in local currency. Factors which might increase private sector liquidity were discussed on page 8. Despite favorable prospects for a gradual increase in liquidity among importers and/or within the banking system in the medium term, and the fact that the grant would presumably be disbursed in two tranches, the $10 million currently does represent the entire deposit base of the commercial banks, and half of the currency issued in Conakry in exchange for the syli in January. It is not surprising that even fairly substantial traders are pooling their resources in order to participate in the auction and to put more pressure on the banks to extend credit to them for this purpose.

Although it is hoped that the volume of foreign exchange trading on the auction will reach and remain steady at approximately $1 million per week, there appear to be no plans to accomplish this by relaxing the 100% cash coverage requirement. Rather, policy adjustments which may be made would apparently focus on local and offshore credit as the means to improve the performance of the auction.

o <u>Credit problem</u>

The current policy of the Central Bank is that the commercial banks should not extend local currency credit for the purpose of participating in the auction. This was clearly stated by the Governor and Vice-Governor and confirmed repeatedly by other interviewees. However, there is no formal (i.e. written) prohibition on such lending. Indeed, at least one bank certainly has provided credit to support bids. At present, however, we are forced to conclude that there is indeed a policy against this practice, evem if the BCRG does not (or cannot) enforce it.

This policy was adopted because the BCRG originally believed that a mechanism would be needed to control excess liquidity and limit credit creation, at least until it had a firmer idea of the size and structure of the money supply and could develop more orthodox credit policy instruments. However, the present illiquidity of the system was not expected.

This current policy against credit is also related to the fact that the BCRG has not yet established what appropriate overall ceilings on domestic credit might be (it would wish credit of this sort to be roughly in line with the movement of the balance of payments), and perhaps to the fear that a sharp increase in leding of this kind would put pressure on the exchange rate, which currently stands close to the level that was hoped for. While it would not be surprising if the policy prohibition were officially lifted at some time in the future, we cannot base our present recommendations on this hypothesis. <u>More importantly</u>, even if the policy were changed, credit in support of auction bids would face the <u>same constraints</u> as any other form of credit, as detailed in Section B above, not the least of which is the uncertain liquidity of the banks themselves. The general liquidity problem would therefore remain at center stage, assuming that the cash coverage requirement (from borrowers' funds or bank advances) remains in effect.

One adjustment which has been discussed by the BCRG and the IMF to render the auction system more flexible would consist in permitting importers to whom foreign suppliers are offering credit terms to cover foreign exchange allocations guaranteed to them through the acceptance of auction bids <u>only as they are disbursed and transferred abroad</u>. Thus, local currency coverage would be governed by the credit terms agreed with the supplier.

In such a case, however, <u>the exchange risk would be borne by the importer</u>. Since the rate has fluctuated thus far by up to 10 per cent, this is still a <u>considerable risk</u> to assume for a short-term transaction. Moreover, only importers capable of +qualifying for offshore supplier's credits would benefit from this adjustment, and presumably there are few traders who presently enjoy sufficiently well-established relationships with offshore suppliers and/or banks to take advantage of the added flexibility.

Another possible adjustment which has been mentioned would be to allow foreign exchange purchasers to invest the funds on the international money market until disbursement to the supplier is required.

b. <u>Other considerations favoring a credit approach</u>

There are other potential benefits of the proposed Phase I credit program which, although more speculative, make this a more attractive option under present circumstances than a sale of the foreign exchange through the auction.

o <u>Support for the development of a credit market</u>

As indicated earlier, even if the banks were unequivocally allowed to extend credit to their clients for foreign exchange purchases and if new funding possibilities were to develop quickly (deposits, discounting facilities, etc.), other constraints would remain on bank lending, not the least of which is their lack of familiarity with and of confidence in prospective borrowers, and vice versa. A short-term hard currency credit program, where the credit risk lies with the BCRG (in a donor grant situation), provides an ideal context in which to encourage the development of credit experience on the part of banks and borrowers alike. Demand for the funds should be high, since it would be in the interest of any importer to seek the loans first, before resorting to the auction. In theory, the funds will be more accessible to smaller traders than in the auction, given the credit element.

o <u>Support for rural marketing and distribution</u>

The credit program may also have an impact on the willingness of importers to extend credit to distributors or the ultimate buyers of their products in the rural areas, since they themselves will have received credit in the first place. It may also encourage them to diversify their activities (as in importing and distributing inputs on credit to producers). However, established "supplier's credit" practices and the constraints to diversification of products and clients discussed in Part II make it somewhat unlikely that any significant progress would be achieved in this area as a direct result of the loans made under this program in the short timeframe involved (the next 12 months or so). Given these constraints, tying the loans to imports of certain products (e.g. agricultural inputs) and/or for sale to c rural areas undoubtedly would defeat the primary purpc providing immediate balance-of-payments support. Ho USAID should actively promote the use of the funds fo such activities and encourage the banks to do so as w they review amnd select credit applications.

c. <u>Description of the proposed Phase I credit progra</u>

The proposed Central Bank credit line would be availa individual borrowers who require foreign exchange to goods. No restrictions would be attached to the t product or source of origin, although USAID and the should promote the most desired uses (e.g. agricu inputs), and it would remain within the discretion banks to approve or disapprove applications within reas

The credit would be extended directly from the Central B the borrowers. The commercial banks would play an imp management role in the process, but would not bear any credit risk since they would be neither borrower nor l They would receive a negotiated management fee fr Central Bank for assuming this management responsib Each of the three commercial banks have expressed willingness to participate in the program. BICIGUI a particularly enthusiastic, although it specifically rec that the management of the program be shared with the banks, given the responsibilities which it has already on.

All three banks are staffed and managed by professional African experience. Management contracts with BIAO for BNP for BICIGUI and Societe Generale for SGBG continuity and quality. It is, therefore, recommende all three banks be invited to participate once it h decided to launch the programme. Spreading the p reduces the burden per bank, and at the same time provic widest cover of suitable borrowers, including those s access to CCCE finance through all the banks, in addit those eligible for IBRD or EDF finance through BICIGUI.

The loan application, management and repayment process described as follows.

- Borrowers seeking import financing under the C Bank line of credit would be qualified commercial banks based on criteria provided Central Bank (agreed upon at the outset with U

- The commercial bank would process the loan application and have the power to appr disapprove such applications.

- o If approved, the commercial bank would draw up a loan agreement between the borrower and the Central Bank. Once signed, the loan funds woulds be disbursed.

- o The commercial bank would then be responsible for supervising and monitoring loan repayment, as in the case of any other credit it would extend on its own account.

- o Repayments of principal and interest would be made into a special Central Bank account, from which a management fee would be paid to the commercial bank.

Loans would be extended to the borrowers at the then-prevailing exchange rate set by the auction. There would be no foreign exchange risk since there would be no foreign exchange debt obligation--the funds would be initially transferred from the U.S. government to the government of Guinea on a grant basis.

The banks would determine the appropriate repayment terms on the basis of normal banking practices. Some could be as short as 3 months where the importation and distribution of fast-moving consumer goods such as rice and sugar is concerned. Others could be for 6 to 9 months where agricultural inputs are concerned and the end-user can only pay at harvesting time.

Under this structure, which could also be applied to the Phase II credit program, loan losses would be deducted from the (already constituted) counterpart fund. There is no doubt that the proposed excercize will entail a considerable amount of risk to the capitalization of the counterpart fund, to which would be added a risk to the speed of its constitution if the BCRG were to insist that it be built up only as the debt from Phase I is serviced. It is inevitable that part of the credits will be lost or only recovered long after the due date.

However, there is no alternative than to rely on the trading houses and on the judgement of Guinea's new banks, which creates an unorthodox and unique opportunity to encourage a private sector which has been suppressed for so long and which is now given the chance to demonstrate its initiative and effectiveness. These trading firms are the only existing and functioning link between port and interior, where they have agents and associates, and they will form the channel for passing on the commodities and the credit that finances them.

d. Conclusion

The recommended approach is based on current conditions which discourage the banks from providing any form of credit (to which is added the policy prohibition on lending for the auction) and which are delaying the flow of local currency into the auction and the banking system. While the auction is simpler to work through and, barring the unforeseen, will produce the desired result of a counterpart fund at least as rapidly as the credit line, USAID has the opportunity here of taking a lead role in encouraging short-term credit creation (where the banks will have to start in any case) and the development of banking relationships within the business community. These objectives will be pursued soon through the local currency credit program, but disbursing the initial grant through a credit line will provide an earlier start to this effort, and under conditions more familiar to the banks than the types of lending which should be the focus of Phase II.

2. Phase II Analysis

During Phase II, the purpose of the credit program will change somewhat. In the initial phase, traders will have been provided with direct access to foreign exchange for import transactions. For the most part, this would require only short term financing, e.g. 3-9 months. Phase II will expand this purpose considerably to fill other key gaps in the availability of credit, some of which would otherwise persist indefinitely (e.g. project financing requirements). Depending on conditions ultimately agreed with the government, the counterpart fund can constitute the basis for:

- short-term credit to finance the trading and distribution of local goods and services of all kinds;
- short-term credit to finance the purchase and collection of export crops for sale overseas;
- short-term credit for the purchase of foreign exchange in the auction (as long as it continues in existence) to import needed inputs; Legal
- medium/long term and/or equity finance to SME's, for example those that qualify for a foreign currency loan under one of the IBRD/EDF/CCCE lines of credit but which are also in need of local currency financing, as will often be the case. Such loans or equity finance will be an extremely useful complement to the foreign currency loans, and their prospective availability has already been warmly welcomed by the representatives of those three agencies;

- medium/long term loans and or equity finance for development finance institution(s) that might be established, e.g. an agricultural development bank which is under discussion at present between the governments of Guinea, France and Belgium and in which additional supporters would certainly be welcomed.

There will no doubt be other productive uses to which the counterpart funds can be applied, and which will become more easily identifiable once Phase I is in train. Part of the technical assistance effort during the initial phase should be to develop and recommend eligibility criteria for the commercial banks to utilize in qualifying projects and borrowers seeking financing from the fund during Phase II.

<u>The management of the fund during Phase II would be the same as that utilized in Phase I</u>. Under this structure, the commercial banks would play the key role in managing the credit program, but would not assume any credit risk since the debt obligations would be extended to the individual borrowers directly from the Central Bank. There are several advantages to maintaining this operating structure:

- the banks would have become familiar with this management and operating structure during Phase I, thus facilitating the operations of the program during Phase II (assuming there is a differential of several months before the latter begins);

- because commercial banks do not generally provide medium and long term debt or equity financing, it will be much easier to encourage them to consider such financing if their risk is minimal; and

- should a decision be made to capitalize a new development finance company, it will be much easier to transfer the counterpart fund into that company if the fund is lodged in a single institution (i.e. the Central Bank) with who USAID can discuss the opportunity, and not divided into distinct lines of credit in several institutions.

Medium and long term lending and equity required in project financing are not traditional commercial banking lines of business. As such, commercial bankers are not trained in analyzing and managing the risks associated with these types of financing. Specialized institutions including merchant banks, development finance companies and venture capital firms have been organized in other countries to provide such longer term, higher risk financing. Part of the technical assistance effort during Phase I should be to analyze and make recommendations on the most appropriate and cost effective institutional mechanism for managing a counterpart fund designed to provide a broad range of financing needs.

3. Technical assistance requirements

The two phase program will require technical assistance of varying types at least over the initial three-year implementation period. Because the types of assistance will vary (summarily described in the following sections) we believe it will be important to have resources available to provide a broad range of assistance as required by the program. Broad categories of assistance that may be required include the following.

- To anticipate, analyze, and propose resolution of any difficulties that might arise between the decision to go ahead with the program and the start of its actual implementation.

- To identify, analyze and propose resolution of problems encountered by the banks, trading houses, individual businesses (borrowers), or USAID during the implementation of either phase of the program.

- To monitor the general progress of the program on a quarterly basis and recommend changes/adjustments that might be required to accelerate disbursements or to better meet changing economic conditions.

- To review, during Phase I, the recommendations made in this report for the utilization of grant counterpart funds in Phase II in light of new opportunities, such as possible plans for the creation of a development finance institution, and recommend needed changes in the overall technical assistance program.

- To review and analyze technical assistance requirements of the private sector in Guinea and recommend where USAID could appropriately and usefully contribute, within the budget for this program or otherwise.

More specific requirements are summarized below.

a. Assistance in the initial grant disbursement exercize

As indicated earlier, almost total reliance would be placed on the commercial banks and the trading houses for the implementation of Phase I of the grant program, which should be underway within the next few motnhs. The banks are professionally staffed and managed, and they will provide short-term credits which is their normal line of business. There appears to be little need for any technical assistance to the banks, therefore, in Phase I.

However, a relatively large number of people and organizations will be involved in the program, which itself will be an unusual excercize in a difficult and fast changing environment. This, in addition to the fact that a large amount of money is involved, makes it likely that a certain coordinating and troubleshooting capability should be available when required from time to time. To address these coordinating and troubleshooting requirements, as well as the assistance needed for the local currency credit program, a firm should be retained to be available in Guinea as required over the first three years of the two phase effort, and starting once USAID has decided to go ahead with the program.

We believe that two specific types of technical assistance will be required during Phase I. First, the Central Bank may require assistance to develop the management and operating procedures to be followed by the commercial banks in implementing the Phase I credit program. Since the objective is to disburse the funds quickly, the procedures should be streamlined. Nevertheless, the commercial banks will require some guidance if they are to be responsible for managing the funds. Topics to be addressed in this effort would include the following.

- o Credit guidelines (eligibility criteria, terms and conditions of loans, repayment guidelines).
- o Commercial bank management responsibilities.
- o Loan mechanics (disbursement procedures, repayment mechanics--from borrower through commercial bank to Central Bank.
- o Documentation requirements.

The technical assistance should be able to address, on short notice, a broad range of credit and management related problems. Those problem areas might include the following during the Phase I effort.

- o Improving coordination between the Central Bank and the participating commercial banks.
- o Streamlining loan procedures and documentation requirements.
- o Improving Central Bank oversight.

- Facilitating the development of relationships between the trading houses and the banks.

b. <u>Phase II local currency credit program</u>

Technical assistance for the Phase II credit program would include the troubleshooting/coordinating requirements begun during Phase I. While the BCRG, the banks and borrowers will have gotten used to working with each other and other Phase I assistance requirements will diminish, there will be new technical assistance needs for the second phase to be successful.

First, the overall Phase II credit program will have to be designed. Because the focus of the second phase will be on project finance (although not to the exclusion of short-term transactions), especially medium and long term lending and possible equity financing, guidelines for utilizing the fund will have to be developed. Assistance will have to be provided at two levels. At the level of the participating banks, assistance may be required in the following areas.

- Operating parameters of the fund
    - Minimum/maximum financing provided
    - Amount of project to be financed
    - Terms and conditions of financing

- Eligibility criteria and security requirements
    - Eligible borrowers
    - Eligible projects
    - Eligible costs
    - Security requirements

- Management and administrative structure

- Financial structure

These last two points are most important if serious consideration is to be given to the possibility of establishing a different type of institution to provide the higher risk financing contemplated during this second phase. Careful analysis would have to be made of the appropriate management, operating and financial structure of any such institution.

At a different level, borrowers may have to be assisted in applying for and effectively utilizing term credit. To the extent practicable and available, the program should tie in to other donor efforts in this area, including any small business assistance programs supported by PVOs, the Peace Corps or others. Effectively utilizing the credit is liekly to require business management assistance in organization-building, bookkeeping, inventory control, receivables and payables management, and in other subject areas.

Second, the trading community in Guinea is in need of training in a number of skill areas. This does not only apply to traders; most private businessmen and (would be) industrialists also have that requirement. At this point in time, insufficient information is available to properly assess what is needed and how USAID could appropriately assist. Several local and international organizations are in the process of developing inventories of the requirements at present, and it is, therefore, recommended that the persons/consulting firm suggested above be requested to address this point and make recommendations when the program is underway.

It is difficult to estimate the exact level of technical assistance that might be required over the initial three year period of the two phase program. Clearly, if substantial new institutional development work is required, the level may be higher than anticipated. For planning purposes, however, we believe a total of $500,000 should be reserved which, over a three year period, might be utilized in tranches of $250,000, $150,000 and $100,000. This should be reviewed at the end of the first year to better estimate requirements during years two and three.

4. <u>Conditions precedent</u>

Before disbursing the grant funds, we recommend that USAID require the government to take several actions which should have a positive impact on the overall ability of the banking sector to service financing requirements:

- make a clear statement of policy as to the extension of credit for purposes of purchasing foreign exchange in the auction;

- make a clear statement as to deposit and lending interest rate policy, and establish a structure if one is to be required, including an indication of minimum time and savings rates and of sectors entitled to preferential lending and discount rates;

- make a clear statement as to overall credit ceilings and any other restrictions to be placed on the development of loan portfolios.

Additional suggestions are presented at the end of Part II.

Comment: [illegible] legal framework for extension of Rural Credit.

PART II - THE RURAL MARKETING AND DISTRIBUTION SYSTEM

A. STRUCTURE AND CAPACITY OF THE PRIVATE MARKETING AND DISTRIBUTION SYSTEM

1. The trading community

The indigenous trading community can be visualized as a pyramid consisting of several "tiers". There are perhaps a dozen "first-tier" businessmen at the top, resident in Conakry, whose local resources and foreign accounts or backers permit them to undertake large import transactions (over $100,000) or to invest in construction, small manufacturing or other ventures. When engaging in commerce, these leading businessmen tend to concentrate on imported bulk food commodities, even more so now that the parastatal network in this area has been completely dismantled. However, they do deal in other imported consumer goods (both mass consumption and luxury items) and are in a good position to diversify even further into a range of agricultural and industrial inputs as warranted by demand. Several of these major businessmen are recently returned exiles.

The second tier consists of leading traders located for the most part in Conakry, Kindia, Kankan (with its strong connections to Mali, Ivory Coast and other points east of Guinea) and Labe (oriented towards Senegal and Gambia in particular). The number of traders in this class is probably no more than fifty to one hundred, including the top half dozen (at most) merchants from other regional capitals. This second tier also engages primarily in the wholesaling of bulk commodities.

The third and fourth tiers represent the majority of licensed merchants, who are considerably smaller than this second tier. The third tier (several hundred individuals) may participate in large bulk commodity import transactions (led by a first or second tier trader, or achieved by pooling together), but essentially for the purpose of supplying their semi-retail shops, which concentrate primarily on these essentials. These merchants however are more likely to deal in a greater variety of consumer goods (e.g. clothing, batteries, soft drinks) than the first two tiers, in which case they may act as wholesalers or financiers to a fourth tier of licensed traders: the "specialists" who are responsible along with a myriad of even smaller importers and merchants (a fifth tier licensed under the simplified procedures of the open air markets) for the vast array of consumer goods available in Conakry and other urban centers.

Finally, the bottom of the pyramid consists of retailers.

One fundamental characteristic of the Guinean trading is the fact that it operates as much on a regional as national basis. Since Guinea produces very few co goods, both large and small merchants routinely buy an goods in neighbouring countries, maintain b relationships there, and in many cases also either o directly within those countries or have family who do. strength of cross-border business relationships is du only to the artificiality of national boundaries inso the ethnic groups involved are concerned, but also t Guinean diaspora which grew to well beyond 100,000 during the Toure regime. Particularly in light o monopolistic nature and inefficiency of the former commercial system and the hostile banking enviro trading patterns and practices within the region reinforced as time went on, rather than di increasingly to direct dealings with industrialized c suppliers from within Guinean borders. Expor definition always illegal under the Toure regime--w substantial component of this trade, with estimate gold, diamond and cash and food crop exports ranging $100 million to $250 million per year.

As in Mali, where liberalization policies have beg succeed in doing so, the hope is that the regional will come out into the open more and pass through of channels, which would be facilitated greatly if the cu were to become fully convertible and if the bankir regulatory systems were to prove that they are the support officially-recorded trade, at a reasonable financially and in terms of the effort required present, much of the impetus in this direction is from Guineans who have returned either from the West o non-trading activities in neighbouring countries, ar are now seeking to engage in commodity and speci trading or in other activities requiring imported inpu capital goods.

The growth capacity of the indigenous commercial appears to be quite high. A clear sign of this potent the fact that licensed traders are organizing themsel influence policy and undertake more sophist transactions. Leading examples are their participation in the development of the new Cham Commerce (created by government decree in May, 1985 bu their considerable input), which reportedly is subsidized, and their establishment of new associ through which they can pool resources for major opera For example, the newly-created Mutuelle de Promotic Commercants consists of 30 members, each representi least 10 others (throughout the country), with each

30 pledged to contribute 50 million FG ($150,000) to a common fund which will initially be used to purchase foreign exchange to deal in the bulk commodities import market, and which could also serve as a loan guarantee fund. Another group, formerly known as the Programme Libre Commerce, consist of a half-dozen businessmen who have 120 distribution points throughout the country. If this type of cooperation can be sustained, it will go a long way towards building confidence, both within and outside the trading community (i.e. on the part of the government, suppliers and financial institutions).

There are other structures which existed already under the Toure regime, such as the Unions (or Syndicats) des Commercants which can be found in all major towns. Their legal status needs to be restated once an associations law is in place (as does that of their members, who are awaiting the issuance of new licenses), and their purposes can be redefined to take advantage of the new opportunities which can be pursued in the liberalized environment. These local traders' associations constitute excellent structures through which credit, training and other forms of support can eventually pass.

A meeting with the members of the Kissidougou traders' association left the impression that it is a tightly-knit group, even though there are substantial income differences between the members. The 20 licensed traders in that town (there have been no newcomers for the past several years) seemed eager to have access to technical assistance designed to help them develop new activities and relationships (e.g. banking) individually and as a group, accounting systems for their enterprises, and so on. Although they are the dominant class at a major crossroads on the edge of the coffee area, only one or perhaps two of them seemed to fall within the "second tier" of fairly substantial traders. There is therefore considerable capacity for expansion and a growth in independence from first and second tier suppliers of bulk commodities, which can be facilitated if they were to pool their resources together on a more regular and ambitious basis. The potential is certainly even greater in a major market such as Kankan or Labe.

Among Guinea's ethnic groups, the Malinke and the Peul are the major licensed traders: even though Kissidougou is essentially a Kissi town, all but three of the traders are Malinke who settled there after independence.

2. Transporters

Nearly all transporters in Guinea are small-scale operators (the vast majority serving all regions are Peul) who own and/or drive at most half a dozen vehicles, principally passenger cars and vans, but also pickups and larger trucks of considerable age and very varied origins. There are a few major fleet owners who have been successful enough to invest regularly in new vehicles (some of these were in evidence in the interior), but most of the smaller entrepreneurs have not done so for many years. There is considerable pent-up demand and apparently some purchasing power even among smaller owners. Many new vehicles reportedly are purchased in Nigeria.

Transporters play a wide variety of roles in the movement of goods within the country and the West African region. They are routinely hired by importers to collect goods in neighbouring countries, or by leading wholesalers to deliver shipments of bulk goods to distributors in the interior. The drivers are sometimes accompanied by a representative of the merchant, but are often trusted to handle the payment to the supplier or from the buyer as well as negotiations with border and checkpoint officials. Their services are all the more valuable because they tend to specialize in certain routes and therefore minimize the risk of loss created by corruption and capriciousness. Since traders rarely own vehicles, they have of necessity developed relationships over the years with certain transporters, more or less as business partners.

Transporters (or at least the drivers) frequently engage in petty trade themselves, haphazardly purchasing crops, charcoal and the like on return trips to urban centers for immediate resale. This practice is bound to become more common and wilful as production and marketing increase. Also, as transport margins become thinner with the rise in fuel prices and increasing competition, they should begin to plan their load strategies more carefully. At present, large trucks regularly return empty to Conakry from the interior. The fact that agricultural production is generated almost exclusively by small farmers makes it inevitable that interested transporters, as opposed to merchants, will have a competitive advantage in an expanding market for local production which they may wish to develop more systematically than in the past.

As in the trading community, local transporters' associations have long existed. They need to be re-established as valid legal entities and encouraged to provide mutual support to their members in dealing with the new banking system and relevant authorities. In Kissidougou, the same group of six transporters have been the officers of the local union for years, and claim to represent some 300 owners. They are all small entrepreneurs--none owned trucks--but they were as enthusiastic as the traders about strengthening their organization and engaging in larger-scale activities. Although union dues are used only for tax payments, it appeared that the organization could generate a fairly substantial pool of capital for use as a guarantee fund or for investment purposes. Transporters may also begin organizing themselves better in order to ensure that they are more regularly supplied with spare parts, tires, and so on than in the past.

Since transporters are still such a distinct class within the marketing and distribution network, and effectively unregulated, they can look forward to earning substantial revenues in the next few years. There are already enormous price differentials between routes (e.g. service on non-paved roads can cost four times more than on paved roads) and different types of activities. All rates reportedly have risen sharply as a result of the recent fuel price increase. Even though rate hikes well in excess of fuel cost increases may not be sustainable over the long term, demand for road transport should be growing steadily throughout the country. Improved planning, financial and management skills will be required if the transporters are to renew their fleets and take advantage of the new opportunities.

3. Producers

In the aggregate, farmers are major wholesalers and retailers. However, individual shipments are small (typically transported by passenger vehicles) and marketing initiatives are the result of immediate circumstances rather than of a planned schedule. The lack of cold storage facilities and transport, as well as the absence of market information and regular intermediaries, make it difficult to organize and time larger shipments. They must wait until a transaction is in hand before harvesting the more delicate crops, or frequently send family members to the regional centers or Conakry who sell immediately in bulk (if the price is right) or remain to sell at retail.

Interviews and secondary sources (such as DAI's recent paper on marketing in the Faranah region) indicate that marketing decisions among producers are generally as sound and as well-informed as is possible under the circumstances. For example, coffee growers in Kissidougou are responding quite positively to the fourfold increase in the official producer price. They are aware of the new competition for their output, and demanding cash rather than the cement which had been offered to them in the 1985 season. This is due not only to the much higher price, but to the fact that less cement is being offered per kilogram of coffee this year than last year (from 1.2 tons to 750 kilos of cement for 100 kilograms of coffee). However, they are still in a poor position to negotiate with merchants (given their lack of organization and transport). Reportedly, false measures are being used and very low prices being paid at some village markets.

The two most experienced groups of producers from a marketing standpoint are plantation owners who have maintained or recovered land, particularly along the coast, and vegetable and fruit growers in the Fouta region. The former are replacing state-imposed cooperatives with newly-formed associations. Some of them have attempted export transactions in direct contact with European buyers (e.g. for the upcoming mango crop) and are seeking to use their land as collateral despite the absence of land and mortgage registration systems. The latter group are Peul smallholders who have been regular exporters of produce to Dakar, particularly citrus, avocado and papaya, and who are known to return from Senegal with fertilizer and other inputs. They are also major suppliers of the Conakry market.

In addition to these two categories of producers, farmers in various parts of the country have the potential to better organize themselves on the market. The Societe des agriculteurs modernes in Kissidougou, most of them tractor owners working fairly large areas (some produce as much as 4 tons of rice), is an example of a group which can provide representation for its members and other farmers in the region, and eventually act as an intermediary. FAO is helping to develop the Groupement des femmes maraicheres in Conakry. Other donor projects mentioned in Part I will be working to develop similar structures for both staples and cash crop producers.

B. RESOURCES AND PROSPECTS OF THE PARASTATAL MARKETING AND DISTRIBUTION SYSTEM

1. Recent policy actions

All Guinean state enterprises in the commercial sector have a limited life expectancy. With the exception of ONAH and perhaps certain activities of ENTRAT, all monopoly rights have been abolished. The fact that up to 50 of them remain technically in existence is due essentially to the time which has been required to organize the World Bank-assisted technical teams which will be carrying out their liquidation or privatization. At the most, half a dozen enterprises may continue in existence beyond the first "disengagement" phase which is now underway, depending on the outcome of diagnostic studies about to be performed. The decisions are being made by the Economic and Financial Coordination Committee (CCEF), of which the lead member for this exercize is the Minister of Planning. World Bank funded consultants and official work groups reporting to these authorities are carrying out the study and implementation work.

The major firms in Conakry (ALIMAG and ALIDI) and in the interior (the 43 ERCOAs) which have dealt in bulk food commodities in the past have already been closed. The surviving state enterprises in the commercial sector specialize in certain product lines (e.g. SONIPE for soap inputs and cleaning materials). Most of them have engaged in only sporadic activity in the past few years and have limited or no current inventories to speak of. New (and short-term) foreign exchange and local currency budgets are being or have been imposed on all of these enterprises: those which have not been dealt with or informed of these budgets (for example, AGRIMA, as claimed by its director) essentially have no plans for the future and are awaiting a decision as to their ultimate fate.

The closure of ALIMAG, ALIDI and the ERCOAs in January definitively turned over the importation and domestic distribution of bulk food commodities to the private sector. Several donors helped minimize the abruptness of this shift, led by France and the creation of the SGC, and the PL-480 program. The lack of confidence in the ability of the indigenous trading community to fill the gap in this sector was somewhat exaggerated, since several groups have aggressively demanded and succeeded in their attempts to share the import and major wholesale business with SGC. For example, members of the former PLC group claims to have imported $4 million worth of essentials since January.

While the closure of ALIMAG and ALIDI did create a void (which was immediately filled), that of the ERCOAs hardly can be said to have done so, since these organizations were supplied on an irregular basis to carry out their commodity and supplies distribution role, and since the policy environment did not favor the production and marketing of the cash crops which they were to collect. Some government and donor officials do argue that the ERCOAs provided a crucial link between Conakry and the interior, even if they provided their services only haphazardly. Indeed, PROSECO, FRUITEX, and other public and parastatal organizations relied in principle on the ERCOAs' local facilities and transport capabilities, having no such resources of their own. However, their own low level of activity (due to agricultural policies and their own operational problems) made this reliance rather academic.

Now that the general environment is improving, the ERCOAs might have played a more useful role with appropriate management, particularly in the short term until the private sector is fully equipped and mobilized to service the rural sector. In Kissidougou, some officials from Conakry were observed making this point by buying coffee at the official price of 400 GF per kilogram, using the local ERCOA warehouse and its trucks.

ALIMAG, ALIDI and the 43 ERCOAs are being audited individually by teams staffed by the ministries of Planning and Finance and supervised by the World Bank consultants. No details were as yet available on how and when their assets would be sold off, although public auctions presumably will be organized to dispose of their warehouses, trucks and inventories if any exist. Problems were being encountered apparently in authenticating their liabilities, some of which are expressed as a debt of barter goods to farmers or traders, including potentially fictitious claims registered in the final weeks before closure.

2. Current status of relevant parastatals

Having eliminated one major area of the state distribution network and proceeding with its liquidation, the government will be turning to case-by-case studies of the disparate 50-odd firms remaining. Below is a brief discussion of the seven enterprises of immediate relevance to the USAID program.

a. AGRIMA AND SEMAPE

These enterprises formerly held monopolies as importers and distributors of farm tools, machinery and spare parts (AGRIMA), and agricultural inputs (SEMAPE), although government line agencies occasionally dealt in these products directly. Originally, AGRIMA handled both sectors--SEMAPE was split off from it in the mid-1970s. Both enterprises report to the Ministry of Rural Development. AGRIMA is the larger organization, with distribution points and employees in each prefecture. SEMAPE has none of either outside of Conakry, and has relied on AGRIMA, Ministry of Rural Development offices and occasionally other organizations to distribute its products--the ERCOAs, COTRA, state farms and, most recently, the Libraport book store network apparently (at least in Mamou). AGRIMA, however, has no means of transport, despite its network: local directors must make their own arrangements in this regard.

Their basic problems are essentially the same:

- o lack of autonomous, effective and technically competent management and lack of coordination with other agencies and projects in the agricultural sector;

- excessive concentration of employees in Conakry--according to the recent study prepared by World Bank consultants for the Ministry of Rural Development, all 56 of SEMAPE's employees and 50 of AGRIMA's 160 employees reside in the capital;

- lack of familiarity with and responsiveness to farmers' needs, although interestingly enough they are still approached by producers, ranging from plantation owners to smallholders, and draw up periodic lists of requests gathered;

- unpredictable budgets--as an extreme example, AGRIMA claims to have imported nothing since the change of regime and to have no budget whatsoever at present;

- complex and lengthy ordering procedures and poor timing in availability of inventory, so critical in agriculture;

- consistently poor procurement decisi-- even if given products imported were app[illegible]e for Guinea, they were not made available necessarily in the appropriate growing area, or spare parts were unrelated to the existing machinery.

In addition to its organizational and logistical problems, SEMAPE has sold inputs at heavily subsidized prices (one-tenth of the actual cost). More often than not, these supplies found their way out of the country to be resold for hard currency and at much higher prices (or sometimes were resold on the local black market)--irrespective of the fact that SEMAPE existed to serve state/collective farms primarily and not the smallholders "market". Besides the perpetual subsidies which it has required to survive, its pricing policy therefore prevented <u>any</u> component of the agricultural sector from gaining experience in the use of inputs, at least as supplied by SEMAPE (see following section). In any case, SEMAPE's turnover has been very modest in relation to potential demand: apparently no more than 3000 tons per year on average. The World Bank's 1984 sector review estimated that the combined average annual turnover of SEMAPE and AGRIMA amounted to only $7 million between 1978 and 1982.

At present, AGRIMA and SEMAPE are still operating, just barely. SEMAPE-supplied fertilizer is available in modest quantities in the Fouta region (and perhaps others). AGRIMA still has left-over spare parts inventories in evidence at various locations (for example, parts for Romanian and Czech tractors in Labe and Kissidougou), and had locally-made scythes available in Labe. Its local directors are attempting to order at least basic hand tools in response to regular inquiries from farmers, although expecting that only a fraction of the volume requested will be supplied. Local AGRIMA facilities, as observed in Kissidougou and reported to be the case elsewhere, have been used by private mechanics in the past year or two, now that the enterprise is resigned to the fact that it cannot provide maintenance services, which the Managing Director stated was in fact AGRIMA's principal mandate and activity in its early years of existence.

Differing opinions about the potential future role of these two enterprises (if any) seemed to hinge on the degree of confidence of the various interviewees <u>in the ability or willingness of the private sector to satisfy demand</u> beyond that serviced by donor or government-run projects, which is the focus of section C below. The weight of the opinion seemed to be in favor of maintaining and reinforcing he enterprises temporarily, and perhaps merging them. Regardless, the two World Bank consultant teams working with the CCEF and the Ministry of Rural Development, respectively, will have taken a much closer look at these two enterprises by mid-1986 and firm decisions should be taken on the basis of their recommendations. These may very well result in the immediate closure of both enterprises.

As far as their potential privatization as entities or liquidation sales of their assets are concerned, several Guinean as well as foreign businessmen have expressed an interest in AGRIMA's network of facilities (and presumably the "goodwill" which somehow has managed to survive as seen in the requests which continue to receive for supplies). AGRIMA's spare parts inventory may prove to be of little use to the extent that most of the primary machinery is beyond servicing. SEMAPE appears to have no fixed assets to speak of.

In addition to taking over where AGRIMA and SEMAPE left off, there is a need for the private sector to get involved in the leasing of heavy machinery (levellers, graders, etc.), a service which heretofore has been provided only by the Public Works authorities.

b. <u>PROSECO AND FRUITEX</u>

These two enterprises held monopolies in the export of cash crops until late December, 1985, principally coffee and palm kernels for PROSECO and various fruits for FRUITEX. They continue to operate, in competition with the private sector, and will also be studied in detail in the next month or two and decisions made. The principal issue which seems to divide opinion as to their ultimate fate is <u>not so much whether (or how quickly) the private sector will be stepping into their roles (although this does remain a concern), as</u>

<u>whether or not their continued operation is needed to prevent the private sector from exploiting producers</u> (i.e. not honoring indicated producer prices).

The latter issue is being overplayed somewhat, since concern is based on the understandably high expectations and chaotic situation created by the simultaneous lifting of PROSECO's monopoly on coffee exports, the fourfold increase in the government-offered price for this product, and the beginning of the harvest season, which all occurred in December-January.

Neither PROSECO nor FRUITEX are equipped to fulfill their roles, which in theory involve not only collecting and processing, but also supplying certain specialized inputs (packaging materials in particular). Neither enterprise has staff posted in the field. FRUITEX owns four trucks, while PROSECO has none. Both enterprises relied to a great extent on the ERCOAs to collect and transport crops to Conakry. Their assets are therefore limited to storage facilities in Conakry and some processing equipment in the case of PROSECO. It is doubtful that they have liabilities to the private sector of any significance.

As exporters, they do have some experience and clients, although sales have been negligble in relation to national production, actual as well as potential. PROSECO is willing to consider new quotes on coffee but appears to have its established contacts among brokerage houses. FRUITEX has experience in exporting pineapples and mangoes to Europe (by air) and in fact has entered into an agreement with a Greek company to build cold storage facilities at the Conakry port to begin shipping product in refrigerated containers. Shipments are taking place on an experimental basis. Both enterprises do have cash available to them (from the 3 billion FG pool reserved for state enterprises in January) to purchase export crops during the current season.

c. <u>ENTRAT, COTRA AND ONAH</u>

ENTRAT (Conakry bulk transport and port clearance), COTRA (bulk transport in the interior) and ONAH (fuel imports, refining and retail distribution) are the three enterprises of note with respect to the transport aspects of the proposed USAID program. ENTRAT and COTRA are of interest because they possess truck fleets which are very much in evidence in Conakry and in the interior. Although COTRA is in theory only expected to provide services to the government, recently it has been openly leasing trucks to private traders when available. ENTRAT owns 67 trucks in fair condition, as well as 10 warehouses.

ENTRAT and COTRA are also on the list of enterprises to be reviewed thoroughly this year by the consultants and work groups supported by the World Bank. While the government originally placed COTRA on a liquidation list in a policy paper last April, its fate is undecided and it could conceivably continue to service the government until a government contracting market develops. With its substantial assets and major responsibilities at the port (however inefficiently and corruptly they are carried out), ENTRAT is less likely to be liquidated soon and may undergo a paring down and restructuring instead. In any case, the monopoly rights of both enterprises in the bulk commodity transport sector have been withdrawn permanently.

ONAH's situation is actively being reviewed at the moment. Negotiations are in progress with foreign oil companies regarding a take-over of the fuel storage and distribution sector, possibly accompanied by the right to import fuel. The opportunity therefore exists for the Guinean private sector to become involved in this strategic area, particularly since the foreign oil companies reportedly did not express a keen interest in rural distribution during the first rounds of negotiation. At least one private Guinean enterprise possesses a substantial fleet of tanker trucks, while ONAH vehicles could be sold off to others.

ONAH has been unable to provide regular and sufficient supplies of gasoline and motor oil to the interior. In Kissidougou, the director estimated that gasoline shipments received averaged only 10,000 liters every 10 days, whereas demand amounts to 15,000 liters per day (there are up to 1,000 vehicles working out of Kissidougou). The chronic shortages are due to both "legitimate" supply problems and a high incidence of theft and diversion of the fuel, which is resold at much higher prices on the black market (quite openly) and in neighbouring countries. The fourfold increase in the official fuel price in January (to 115 FG a liter, still well below that of several neighbouring countries and no more than 30% of the black market price) and the creation of a special control corps managed by the Ministry of Commerce have had no dampening effect apparently on this leakage from the official network and from Guinea.

Rural fuel distribution is therefore a major strategic problem area. Comprehensive reforms at the policy level and restructuring upstream in the distribution network are needed before the private sector can step in to take over the transport function and existing service stations on a profitable basis. The outcome of ongoing discussions over the partial or total privatization or liquidation of ONAH is therefore a key determinant of the future national strategy and structures in this sector.

C. PROSPECTS FOR DIVERSIFICATION IN SUPPORT OF AGRICULTURAL DEVELOPMENT

The ultimate objective of the USAID local currency credit program is to encourage the growth and diversification of the rural marketing and distribution system. As stated at the beginning of Part I, it would be unrealistic and premature to exclude any major segment of the Guinean private sector from the credit and technical assistance aspects of the program. The participation of large experienced traders who deal at present only in bulk commodities is just as necessary as that of local farmers' associations. Importers, distributors and the producers themselves should all be eligible to borrow, and the actual use of the funds in the early turns of the line (at least the short-term loans) should be secondary in relation to the process of sensitizing participants to the need and opportunities for diversification into production-related marketing. This can be achieved through effective promotion of the program's objectives by USAID and the banks.

The trading community currently does not deal at all in agricultural inputs. With the exception of the rush for coffee this season, the first four tiers hypothesized in section A above (i.e. licensed traders) also do not deal in agricultural produce as a regular line of business. Smaller merchants, particularly those with ties to the Fouta region and other produce-growing areas, do move shipments to Conakry on a fairly regular basis, or purchase them wholesale when delivered to Conakry and other major centers. Producers themselves are active marketers and even exporters, but on a small scale when disaggregated. As noted, transporters are also intermittent purchasers of produce.

At present, there are are both "positive" and "negative" constraints to diversification away from consumer goods marketing in the trading community:

- Positive constraints relate to the fact that the consumer goods sector is thriving, with considerable room for growth.
- Negative constraints stem from the lack of experience and other conditions of historical origin within the system which disfavor agricultural input and output marketing.

1. Positive constraints

The focus of licensed traders is on the six essential bulk food commodities (rice, oil, sugar, flour, tomato paste and powdered milk), a few other mass consumption items and certain more specialized consumer product lines. This concentration of activity was greatly reinforced by the complete withdrawal of the government from the market, and by its concern that there be no real or artificial shortages during the initial transition period, and as little inflation as possible. Traders have received extra encouragement to step into the bulk food import market by the fact that they were allowed up to now to buy foreign exchange in the auction at the rate of 300 Guinean francs to the dollar, otherwise reserved for the state and mining sectors. This particular incentive was scheduled to disappear in April, when all transactions were to be subject to the weekly auction-determined rate of exchange.

Trade in mass consumption items is very profitable, particularly for importers and major wholesalers. What few price controls exist (e.g. on imported rice) are not being enforced or respected, and this is clearly a sellers' market at present. The prospect of immediate, substantial gains is therefore a major factor which is keeping the scope of mass trading activity as narrow as it is. Even where margins are low, as in the case of "third tier" traders such as the members of the Kissidougou association, volume is sufficiently large to warrant concentration on the six essential food commodities (and perhaps cement). Shipments of 50 to 100 tons of flour or sugar are not uncommon in a town such as this, where they are handled initially by a perhaps five or six of the 20 resident traders.

The fact that these are such basic, fast-moving products virtually eliminates commercial risk and keeps operations simple: very little planning, management or marketing is required, at least at the local distributor's level. Nevertheless, the top two tiers of traders are working with growing networks of distributors, which are increasingly challenging to monitor.

Thus, the policy environment, the volume and profitability of this trade, its straigthtforwardness for smaller traders and its increasing complexity for larger traders all favor a continued concentration of activity in the consumer goods sector.

2. Negative constraints

The major negative constraints to increased trading in inputs and produce are summarized below.

a. The general lack of information

There is no firm statistical information available in Guinea on agricultural production, produce price fluctuations and consumption volumes, input utilization, export markets, and

so on. For example, the FAO has b
of 20 vegetables and 12 fruits at
for the past year, and plans to exp
major markets. This is the first e
independence and even this info
available. The statistics show ext
volume (not claimed to be reli
reliable) from month to month.

On the input side, the World Bank
to require as a condition of its s
that the Ministry of Rural Developm
a system to track and project
Estimates of current effective d
8,000 to 50,000 tons per year.

b. Potential competition fro

In the past, inputs distributed
subsidized. There is a strong con
expressed in the PIRN (interim na
that this practice should cease i
pressure to build effective dema
introduce improved technology ra
effort. Both government and donor
export trading partners in the
provide inputs at less than worl
who have been following the s
concern over the possibility that
subsidized competition in the nex
in areas in which demand might
higher-value cash crops are produ
subsidized inputs smuggled out of

c. Problems of demand and e

The literature indicates that ther
demand for and experience with inp
in certain well-defined areas
owners in the coastal region). H
is of little significance, since
were available in the past were as
market prices. Although farmers
inputs and some are committed enc
own supplies, many interviewees ar
demonstration effect from developm
assistance in general could creat
viable market. This is viewed as
programs which would merely increas
producers, although the extension
a useful incentive to experimentat

The lack of experience with inputs of both farmers and traders also make it unlikely that a free market would develop quickly. The technical nature and great diversity of products, as well as the seasonality of potential demand, are factors which would make it difficult for traders one the one hand to develop a steady line of products and on the other hand to operate at full capacity year-round. Coupled with their lack of experience, these considerations raise perceptions of risk considerably. However, if the demand is there and identified with sufficient precision, which could happen soon once technical packages now being introduced prove their worth to farmers, the trading community ultimately will respond. It is quite likely, however, that they will require cash until producers' are sufficiently organized to purchase inputs in bulk.

On the produce marketing side, leading traders have little experience with cash crops, having never been allowed to export them prior to 1986 or seen any interest in competing with the smaller-scale traders, transporters and producers who sell them on the domestic market. The "second- and third-tier" traders in the Forest Region did however begin collecting coffee on behalf of the ERCOAs in the last year or two of their existence (once barter terms had become attractive) and therefore have acquired some experience in identifying and dealing with producers. In any case, the major traders are now without question looking for export opportunities: if the demand is there internationally, as in the case of coffee this year, they are willing to set up substantial buying operations.

d. <u>The problem of transport</u>

Transport appears to be readily available for established trade routes,. However, there is clearly a lack of adequate service to more remote areas, and certainly no enterprises specializing in bulk transport of cash crops, due to the absence of feeder roads and to past disincentives to or prohibitions on private production and marketing. Even along the major axis between Conakry and Kissidougou, one encounters almost no crossroads. Although this constraint cannot be eased rapidly, the more favorable policy environment is creating immediate opportunities for transporters, since traders and producers typically do not own vehicles. For example, truck leasing activities have been brisk during the current coffee season.

Although transporters could also play a more strategic role than they do now as a distinct class of intermediaries acting for their own account, they have apparently not become involved as direct purchasers in this first season of open trade in coffee.

D. PROGRAM DESIGN CONSIDERATIONS

The USAID credit program aims to make a lasting contribution both to the development of the credit market and to diversification in the rural marketing and distribution system. Research for Part I demonstrated that local currency credit could be put to many relevant uses in making this system more responsive to rural production-related needs (ranging from short-term loans to purchase export crops or foreign exchange for input imports, to long-term loans for vehicle purchases, to helping to capitalize a new development finance institution). All segments of the private sector--traders, transporters, farmers and manufacturers of relevant products--have a potential role to play in supplying inputs and/or marketing crops in Guinea or abroad.

Part II demonstrates that what the private sector needs most in order to turn towards these types of activities is a clearer concept of the potential which lies there, as well as better organizational structures, particularly among themselves, both of which would allow them to experiment and take more risk. Conditions precedent to disbursement of the USAID grant, the credit program itself, and the technical assistance should therefore focus as much as possible on promoting institutional development within the private sector.

1. Conditions precedent

We recommend that USAID require the following action to be taken by the government before disbursing the first tranche of the grant (assuming that this would be as early as July or August):

- o adoption of a new associations law covering cooperatives and organizations such as the Mutuelle des Commercants.

Prior to disbursement of the second tranche, the government should have taken the following actions (assuming this would be by January, 1987):

- o adoption of a revised Commercial Law and a new Investment Code;
- o a firm decision on the future role (if any) of PROSECO, FRUITEX, SEMAPE and AGRIMA; and
- o adoption of a plan of action for the establishment of a land title registration system, and actual establishment of a registration system for vehicles and for liens on all forms of collateral.

All of these conditions are on the agenda within the indicated time frames, but additional reinforcement would be appropriate. Also, USAID might wish to consult with other donors concerned with institutional changes which are likely to occur within the government during the time frame involved, particularly within the Ministry of Rural Development, the Ministry of Commerce and ONAH, which might be of relevance to the program.

2. <u>Orientation of the credit program and its technical assistance</u>

Part I recommended that eligibility requirements for the local currency credit program be examined in detail and agreed upon with the government and the banks during the early weeks of disbursement of the grant, or sooner if possible, since advances could be made to the counterpart fund as soon "Phase I" begins, providing for an immediate start to "Phase II". The range of authorized transactions will certainly be quite broad, given the diversity of needs and opportunities.

However, it is entirely appropriate that USAID indicate a preference for certain types of activities, directly and through the banks, and that the technical assistance team help create appropriate conditions to make these activities more attractive. A particularly useful purpose which the program could serve is to encourage the <u>further development of traders', transporters' and farmers' associations and their introduction to the financial market</u>, as borrowers and as guarantors of debt. With respect to input imports and crop exports, the larger the transactions which the system is capable of putting together, the more likely that the international trade transaction will occur, since the process involves linking a large number of producers to sources of supply or purchasers abroad. Indigenous structures clearly need to be developed to provide the necessary intermediation. This is an area in which the technical assistance can bring about concrete, lasting results.

Another recommendation which was frequently encountered, but which is difficult to support in principle or in practice, is that USAID attempt to concentrate the resources which it is making available in certain regions. Although it is certainly tempting to consider working primarily on the redevelopment of plantations in the coastal region or to collaborate with other donors in the Fouta Djallon, much of the incentive effect of the program in terms of encouraging new forms of institutions to develop and be replicated would be lost. However, it would certainly be appropriate for the banks to develop ongoing relationships with certain borrowers and to take advantage of growing familiarity with certain regions (particularely those where BICIGUI will be establishing branches).

3(A)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.

A Congressional Notification was forwarded to Congress on May , 1986.

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?

The Conditions Precedent to disbursement and covenants contain requirements for the enunciation of domestic credit policy and the issuance of revised commercial and investment codes.

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

No. The assistance is being provided directly to the GOG because of the U.S.'s desire to support certain policy reforms undertaken by the

is assistance not so given? Information and conclusion whether assistance will encourage regional development programs.	Government. The U.S. believes these reforms are necessary to the improvement of the Guinean economy.
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.	The Guinean EPRP is designed to support policy reforms that will encourage private sector development in the agricultural sector. As a condition precedent to receipt of assistance, the GOG must eliminate all subsidies to government-owned and operated agricultural institutions which give those institutions an unfair advantage in competition against the private sector. The GOG has also agreed to adopt a comprehensive credit policy, and Tax and Customs Codes that encourage private sector development.
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).	A U.S. accounting firm will provide technical assistance under this Grant. In addition, the strengthening of the Guinean private sector will encourage U.S. investment in what was previously regarded as too risky and ill-defined an economic environment.
6. FAA Sec. 612(b), 636(h); FY 1986 Continuing Resolution 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.	Not applicable under this assistance.
7. FAA Sec. 612(d). Does the U.S. own excess foreign currency of	No.

the country and if so, what arrangements have been made for its release?

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, the selection of a Technical Assistance Contractor will follow AID-direct contracting procedures which require advertising and full and open competition.

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 AID funds?

Not applicable.

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 NONPROJECT 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. It will promote economic stability by providing the foreign exchange required for Guinea's development and stability.

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

No.

c. FAA Sec. 531(d). Will ESF funds made available for

Yes, local currencies will be used to provide loans to 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?

businesses in the agricultural sector in order to encourage increased food production and to move Guinea toward self-sufficiency in that area.

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?

Not applicable.

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 AID, of the ability of likely recipients to use such spare parts and imports in a maximally productive, employment generating, and cost effective way;

(ii) imports shall be coordinated with investments in accordance with the recipient country's plans for promoting economic development. AID shall assess such plans to determine whether they will effectively promote economic development;

Not applicable.

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

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

(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;

(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 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.

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 America (the "Treaty of Tlatelolco"), cooperates fully with the IAEA, and pursues non-proliferation 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?	Not applicable.

2. Nonproject Criteria for Development Assistance

a. FAA Sec. 102(a); 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	Not applicable (ESF funds used).

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, and 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 economies of developing countries and the improvement of women's status; and, (e) utilize and encourage regional cooperation by developing countries?

b. FAA Sec. 103, 103A, 104, 105, 106, 107. Is assistance being made available: (including 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.)

Not applicable.

(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; [103A] 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

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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.

(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.

(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.

(4) [106] for technical assistance, energy, research, reconstruction, and selected development problems, if so, extent activity is: (i)(a) concerned with data 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 development activities, especially with U.S. private and voluntary, or regional and international development, organizations;

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

(iv) reconstruction after natural or manmade disaster;

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

(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.

(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.

Not applicable.

c. <u>FAA 118(c) and (d)</u>. 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?

Yes, pursuant to AID Reg. 16, the Guinea EPRP Program is categorically excluded from the necessity of further environmental review. The determination granting the categorical exclusion is attached as an Annex to the PAAD.

d. <u>FAA Sec. 281(b)</u>. Describe extent to which the activity

The activity supports the economic reform and public 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.

administration decentralization program of the GOG which aims to encourage increased participation of individuals in the development of the country.

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. The activity supports previously initiated economic reform program focused on the liberalization of the economy and the development of the country's resources.

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ANNEX III

Phase I (before 1/06/86)	Phase II (1/06/86-12/31/86)	Phase III (1987-)
Monetary/Exchange Rate Policy		
Restrict foreign exchange activities of specialized banks <BCRG>(09/11/85) *	Extend floating, market-determined exchange rate to all transactions through foreign exchange auction <BCRG> (3/31/86) *	Examine possibility of reentry to Franc Zone
Open "second window" for foreign exchange operations <BCRG> (10/07/85) *	Introduce Guinean Franc (FG) <BCRG> (January 1986)*	
Create new commercial banks (August-December 1985)	Agree on program for liquidation of state banks <BCRG> (03/31/86) #	
Suspend banking operations of state-controlled banks (12/23/85)		Introduce more specialized banking functions and other financial sector reforms
	Credit and money supply ceilings <BCRG> *	
Reorganize Central Bank (September 1985) *	Multilateral debt rescheduling <MPCI> (first quarter 1986) #	
Price Adjustment and Market Liberalization		
Abolish forced marketing of agricultural products (April 1984)	Adjust prices of rice and petroleum quarterly to reflect import prices and exchange rate movements <SEC, MDR> #	Annual review of coffee and palm kernel prices <MDR,SEC>
Abolish state cattle marketing agency and state collective farms (April 1984)	Adjust public utility prices quarterly to reflect cost of production, especially imported inputs <SEE>	Progressive disengagement of Government from rice and petroleum import, handling and storage
Remove road controls between the regions (May 1984)		
Decontrol of producer prices (1985 season)		
Announce new coffee/palm kernel prices <SEC, MDR> (12/16/85)	Adjust coffee/palm kernel prices <SEC, MDR> (6/30/86) #	
Increase prices of rice and petroleum to reflect import prices and new exchange rate * <SEC, MDR> (1/06/86)		

* denotes IMF condition. # denotes Second Tranche condition.

Phase I (before 1/06/86)	Phase II (1/06/86-12/31/86)	Phase III (1987-)
Agricultural Sector		
	Formulate procedures for monitoring fertilizer use (3/31/86) <MDR>	Takeover by private sector of all input supply and marketing activities
	Review rice stocking and distribution arrangements (06/30/86) <MDR,SEC> #	
	Review supply and distribution of agricultural inputs, and propose action program to ensure 1986/87 supply <MDR> (06/30/86)	
Tariff Reform		
	Introduce simplified tariff structure <MEF,SEC> (1/31/86)	
	Replace import licensing procedures with import declarations handled through commercial banks <SEC> (1/31/86)	
	Review appropriateness of tariff structure and effectiveness of customs procedures <MEF,Industrie> (11/15/86)	Further revision in light of rates in neighboring countries <MEF>
Economic Environment for Private Investment	Promulgate Mining Code <MRNEE> (1/31/86)	
	Revise Commercial Law <SEC> #	Review investment environment, especially financial sector <MRNEE,BCRG>
	Promulgate Petroleum Code after comparison of production sharing vs joint venture arrangements <MRNEE> #	
	Promulgate revised Investment Code and application procedures <MPCI> (6/30/86) #	

* denotes IMF condition. # denotes Second Tranche condition.

Phase I (before 1/06/86)	Phase II (1/06/86-12/31/86)	Phase III (1987-)
Public Sector Management and Reform		
Unification of Government budget and transfer of external debt management to MEF (09/11/85)		
Formulate new public sector procurement regulations <CNMP> (11/30/85)	Implement new Government procurement procedures, <CNMP> (01/31/86)	
	Review external borrowing procedures/policy <MPCI,CCEF> (11/30/86)	
Undertake civil service census and study of Government organization <MFPRA,MPRND> (August-December 1985)		
Remove public enterprise employees from civil service rolls <MFPRA> (12/23/85)		Adjust civil service salary scales <CGRA,MEF> (01/01/87)
Introduce salary compensation for rice and transport <CGRA,MEF> (1/1/86)	Reduce public employees by a further 10,000 staff <CGRA> (06/30/86) #	
	Pay salaries and rice allowances of staff placed "in reserve" for six months following lay-off <CGRA,MEF>	
	Review proposals for decentralization of Government operations and revenue sources <CGRA,MEF>	Implement decentralization of Government functions <CGRA> (1987-89)

* denotes IMF condition. # denotes Second Tranche condition.

Phase I (before 1/06/86)	Phase II (1/06/86-12/31/86)	Phase III (1987-)
Public Investment		
Restricted 1986 Public Investment Program (limited to completion of on-going, viable projects) <MPCI>	Undertake no new investment in public enterprises or mixed companies except in context of agreed rehabilitation projects <CCEF>	Start implementation of new strategies and investment programs <technical ministries> under revamped monitoring procedures <MPCI,MEF>
	Complete and review master plans and sector investment strategies for: Agriculture <MDR> Power <SEE> Water <SEE> (06/30/86) and Transport <SET> (09/30/86)	
	Complete education and primary health sector strategies before new investments are undertaken <MEN,MSPPAS>	
	Introduce three-year investment programming with new procedures <MPCI>	

Phase I (before 1/06/86)	Phase II (1/06/86-12/31/86)	Phase III (1987-)
Parapublic Enterprise Reform		
Prepare and approve parapublic rationalization/divestiture strategy and action plan. for industrial enterprises <CCEF> (11/30/85)	Establish a plan for restructuring the non-industrial parapublic sector <CCEF> (3/31/86)	Review and enhance incentives for private sector job creation
Liquidate 19 industrial and 4 non-industrial public enterprises, and EPCOAs <CCEF,MDI,MC,MPRN> (12/31/85)	Carry out rationalization programs per agreed schedules <CCEF>	
Agree public enterprise working capital, credit and foreign exchange provisions while sector is being restructured * <CCEF,MEF,BCRG> (12/12/85)	Review statutes of public utilities (power, water, telecommunications) and take remedial legal action to amend if needed <CCEF,SEE,MCT>	
Suspend Air Guinée's international services * (1/2/86)	Revise autonomy provisions in port, airport and railway statutes <SET> (04/30/86)	
	Revise mining sector legal and taxation arrangements <MRNEE,MEF>	
	Revise Air Guinée statute <SET> (06/30/86)	

* denotes IMF condition. # denotes Second Tranche condition.

Annex IV

Foreign Exchange Auction
Actual Operations
(U.S. Dollars)

Date	Sold	Bought	Rate
1/28/86	721,000	-	355
1/31/86	96,800	-	370
2/7/86	33,526	-	365
2/14/86	502,382	225,000	370
2/21/86	666,000	-	350
2/28/86	684,960	-	340
3/7/86	1,675,000	-	340
3/14/86	370,000	-	345
3/21/86	518,860	-	345
3/28/86	1,024,197	240,000	350
4/4/86	844,900	-	360
4/11/86	249,605	-	365
4/18/86	1,411,170.59	28,000	355
4/25/86	1,060,268	1,951	345

Source: Central Bank of Guinea

ANNEX V

Macroeconomic Framework:

1. Economic conditions and growth prospects:

Guinea's economic history during the past twenty-eight years is characterized by a sharp and continuous reduction in production, especially agricultural production. The primary reason for this decline is the failure of the past policies that were aimed at promoting the role of the state in all sectors and the resulting neglect of smallholder agricultural production, the source of the bulk of Guinea's total output. Previous policies were dominated by the objective of keeping the purchasing power of urban civil servants high at all costs. The disincentives faced by smallholders during this period include lack of access to credit, production delivery quotas to official agencies at unfair prices, lack of access to appropriate technologies and production inputs, and unavailability of consumer goods in rural areas. As a result, farmers shifted production from cash crops to food crops to meet their subsistence needs. The declining export crop production was usually diverted to parallel market operations which decreased official export earnings and raised domestic consumer prices.

The other major sector in the economy, mining, is now the primary source of Guinea's foreign exchange earnings. Guinea is almost exclusively dependent, 97% of all foreign exchange earnings, on exports of bauxite and alumina. Although demand and output rose in the mid 1970's, demand for both has stagnated since that time. Total exports also fell, although there was a slight recovery for bauxite in 1984 when 12 million tons were exported, an increase of approximately .8 million tons over the 1980-1983 average. Alumina exports fell during the same period from a high of .715 million tons in 1980 to .532 million tons in 1984. Falling world market prices for both will, however, negatively affect the GOG's foreign exchange earnings and reform efforts.

Other minerals include diamonds and gold. Diamond production rose from 6,000 carats in 1980 to 40,000 carats in 1983 because of the GOG's policy of allowing private miners to receive 40% of their proceeds in foreign exchange. Production declined to 23,000 carats in 1984 but this can be at least partially explained by the excess in world-wide production and the resulting fall in international diamond prices. Private Guineans were, however, excluded from engaging in diamond mining activities in 1985. Since 1984 industrial diamond mining has been carried out by a joint venture, 50% GOG and 50% AREDOR a group of foreign private investors. Original annual production estimates of 260,000 carats were recently revised upwards. Gold is presently mined by small prospectors who smuggle production abroad. The GOG intends to set up a purchasing agency to capture part of this production for official channels.

The manufacturing and industrial sectors were and remain dominated by public enterprises and consisted mainly of agro-industry, construction, chemicals and textiles. These enterprises consumed approximately 15% of total public investments between 1970-1985. Unfortunately due to poor management, lack of spare parts and raw materials, irregular electricity, lack of foreign exchange, overstaffing, and minimal maintenance, the companies only operate at 15% of installed capacity. The estimated 160 million GF operating deficit was subsidized in 1984 by the Government. Losses through early 1986 following exchange rate adjustment and the continued inefficient operation of most of the enterprises are estimated to total 9.6 billion GF or $32 million.

Economic conditions in Guinea are rapidly changing. Economic growth has been consistently below 3% since the mid-1970's with bauxite operations expanded. The economy was dominated by the public, official, sector which accounted for approximately 25% of GDP.

This sector was characterized by an overvalued currency with controlled prices linked to the currency. Approximately 90,000 civil servants and public enterprise staff were employed by the public sector. The remaining 75% of GDP came from parallel market activities. These activities, operating openly since the end of the 1970's accounted for almost 80% of urban consumer demand in Conakry and almost 100% of marketed consumer goods outside of Conakry!

The poor performance of the public sector, especially that of the public enterprises, led to the virtual collapse of the economy. As a result, the GOG prepared and began implementing in December 1985 a far-reaching economic reform program. The objective of the program is to liberalize the economy and to support the growth and development of the private sector. During the past six months, the GOG completed its exchange of currency exercise during which time almost 30 billion sylis were exchanged for the new franc Guinean. The new currency was devalued by 1500% with subsequent weekly adjustments made through the foreign exchange auction at the Central Bank. This new system allows the commercial sector free access to official foreign exchange. The previous banking system consisted of six state owned banks. The state banks were closed December 23, 1985 and their assets are presently being liquidated. Three new banks with foreign and private participation were opened in 1985. These banks were responsible, along with the Central Bank, for managing the currency exchange exercise. The Central Bank is being reorganized to improve its operations and to enable it to undertake increased responsibilities.

Producer prices increased for coffee and palm kernel from 80 to 400 GF/kilo and 18 to 60 GB/kilo respectively. The consumer price of rice rose from 20 GF/kilo to 80 GF/kilo. Locally produced rice and other food crop prices were also decontrolled.

Gasoline prices went from 30 GF/liter to 115 GF/liter. Another increase in gasoline prices to approximately 150 GF/liter is expected shortly. Negotiations are presently underway with representatives from seven oil companies on their participation in a mixed company to import petroleum products, control storage at the port, and distribute at the wholesale level. Retail sales will be handled by the private sector. Public transport tariffs were increased from 15 GF/ticket to 40 GF/ticket. Electricity rates are expected to increase from 6 GF/kilowatt hour to 54 GF/kilowatt hour for the general public and 64 GF/kilowatt hour for commercial users later this Spring. Meters will be installed for all customers. Nineteen public enterprises were liquidated while the remaining thirty-five presently under review have been divided into three categories: eleven that may be retained, seventeen for which buyers are being sought, and seven to be liquidated.

The economic prospects for Guinea are beginning to improve. The GOG has seized its opportunity and begun ambitious reforms. The fall in oil prices will result in a considerable decrease in its oil import bill this year. Cheaper oil means that more foreign exchange will be available to finance essential imports, rebuild foreign exchange reserves, and service national debt. The recently concluded Paris Club Meeting resulted in the rescheduling of 95% of Guinea's arrearages, principal, and interest. This improves the country's credit worthiness and opens the way for the inflow of additional resources. The GOG has started to shift from import substitution to exports. The GOG is actively seeking foreign investment while working to improve the climate for increased local and less capital intensive investment. Farm gate prices increased. All these actions will have a positive impact on the economy if the reform program remains in effect and if investors, farmers, and traders respond to them.

Lack of incentives to producers, administrative rigidity and corruption of the public sector have characterized the Guinean economy. As a result, investment and growth rates remained low in comparison with the country's potential. With the foundation laid by the reform program, Guinea's medium to long term growth prospects are considerable in spite of the present economic and financial crisis. Soil, water, and climatic conditions, in normal times, allow the country to not only be self-sufficient in food but also to become a major exporter of a wide variety of citrus fruits and vegetables. Livestock production is wide spread in middle and upper Guinea. The elimination of taxes and monopolistic purchase and sales regulations, livestock production is expected to increase rapidly. Mineral and energy, resources, outside of bauxite, remain largely unexploited. The drastic changes underway because of the economic reforms will enable the Government to begin the development of these resources.

2. Fiscal Position:

The GOG's financial crisis is attributed to the poor performance of public enterprises and the increasing role of the private sector in unofficial trade. Starting in the early 1980's with the liberalization of imports of consumer goods, tax and customs' receipts fell. Non-tax revenue transfers from public enterprises to the national treasury also declined because of the fall in profits. Budgetary transfers to support the operations of the public companies continued. Increased efforts by the government to collect taxes and improve customs operations led to increased revenues in 1984. After a 40% fall in revenues in 1983 to just over 10 billion sylis, (due to repayment of taxes in 1982), government revenue rose to 11 billion in 1984. This increase reflects private sector optimism following the establishment of the Second Republic as well as intensified GOG efforts to collect overdue taxes.

Shifts in government expenditure levels are the result of transfers from the treasury to public enterprises. Thus, while overall government expenditures were 19.6 billion in 1982 they fell to 13.3 billion in 1984. This reflects direct transfers to public enterprises which jumped from .6 billion Guinean sylis in 1981 to 5.5 billion in 1982. Transfers held steady at 5.8 billion in 1983 but declined to 2.8 billion in 1984. The transfers financed the bill for imports of consumer and capital goods. Other government expenditures fell between 1982, 3.8 billion GS, and 1984, 2.1 billion GS. This decline is the result of the completion of the OAU conference projects and the Second Republic's investment plan.

The budget deficit continued to worsen in 1985 when it reached 12.3 billion GS or 135% of total revenue. This deficit is the result of the continued poor financial management performance of public companies. Transfers from state enterprises declined by 1 billion GS from the previous year to 155 million GS. Corporation tax payments, excluding the mining sector, fell 50% to 450 million GS. The collection of other taxes increased, led by import taxes which registered a 12.5% increase over 1984, an exceptionally good year.

The exchange rate adjustments are expected to make a favorable impact on government revenues in 1986. The elimination of subsidies to public enterprises should enable the GOG to improve its budgetary position, make increased contributions to financing investment programs, and, with favorable debt rescheduling from its creditors, become current on its arrears. The GOG must, however, take into account the projected fall in earnings from bauxite exports and hold compensation payments to departing civil servants to levels that will not adversely affect its budget.

3. Balance of Payments Position:

The overall balance of payments position was negative with substantial deficits recorded between 1981 and 1985. The growing deficit is the result of the accumulation of foreign debt obligations. These obligations were greater than Guinea's ability to meet debt service payments. External borrowings were used to finance investments in infrastructure and public enterprises. Outstanding public external debt reached $1.6 billion at the end of 1984. At that time, the ratio of scheduled debt service obligations to total official export earnings was 34%. Actual debt service payments amounted to only 20%. Debt service on private, non-guaranteed debt was $180 million or 11% of total official exports in 1984.

In 1985, higher services and private transfer payments combined with lower inflows of public transfers and led to an increase in the current account deficit. Net inflows of public transfers occurred in 1984 because of exceptional aid assistance related to the earthquake in late 1983 and increased aid to the new Government in 1984. The growing deficits were financed by reducing official reserves and increasing the payments of arrears or medium and long-term public debt. By the end of 1985 official reserves were estimated to be the equivalent to less than the value of one week of public sector imports.

The need for increased funds to finance imports to rehabilitate the economy and the projected lower demand and price for bauxite require the GOG to rapidly expand non-bauxite exports and control food imports if the GOG's short to medium-term objectives are to be obtained. Lower bauxite earnings, should, however, be offset by a decline in the value of rice and petroleum imports.

In order to obtain the time and resources needed to expand its non-bauxite exports and to reform its economy, the GOG met with its Paris Club creditors in April to refinance its external debt, particularly the arrears. The negotiations were successfully completed with 95% of principal and interest due from January 1, 1986 to February 28, 1987 rescheduled or refinanced. The Guinean authorities are currently discussing debt relief with other major creditors, including commericial banks. All of the remaining creditors are invited to attend a meeting of the Conakry Club in May at which time the GOG hopes to obtain debt relief on terms comparable to those of the Paris Club.

The debt rescheduling and refinancing exercises are, however, only part of the assistance that the GOG will need if the reform program is to succeed. New and substantial amounts of balance of payments assistance on concessional terms and debt relief are required to offset projected deficits of $169 million in 1986, $165 million in 1987, and $100 million in 1988 and 1989. Increased assistance is critical during the first two years of the reform program as the GOG attempts to increase the importation of capital and intermediate goods for new investments and the rehabilitation of existing assets. Additional funds will also be required to fund the consumer goods imports to provide incentives to the rural areas to increase agricultural production above subsistence levels and to redirect exports into official channels. If Guinea's immediate external assistance requirements are met during the reform period and succeeds in diversifying its exports, the country's current account deficits should become sustainable in the 1990's.

Annex VI
Trade Payments and Capital Flows
1985-1986
(US $ Millions)

Balance of Payments	1985 (estimate)	1986 (projected)
Exports	559	538
Imports	448	511
Trade Balance	111	27
Services and Private Transfers (net)	-191	-195
Interest M & L/T Debt	(-53)	(-12)
Workers' Remittances	(-10)	(-46)
Current account, ex transfers	-80	-168
Official Transfers (net)	23	28
Balance on Current Account	-58	-139
Foreign Investment	40	45
Net M & L/T Borrowing	-33	-48
Disbursements	109	118
Amortization, scheduled	-142	-167
Short term capital net	-12	-10
SDR allocation	-	-
Errors and omissions	6	-
Overall Balance	-57	-169
Financing:		
Use of IMF Credit	-	-6
Increase in arrears	46	-
Change in Reserves (- = increase)	11	-11
Net reserve level	-216	-205
SAC and SAC related financing	13	123
SAC, SFA	-	39
SJF (Germany, Japan)	-	35
IMF Stand-BY	-	31
Bilateral Aid (Switzerland, France)	13	18

Source: World Bank

Annex VII

Composition of Exports
(in millions of U.S. $)
(constant 1982 prices)

	1982	1983	1984	1985	1986	1987	1988
Total Exports, FOB	453	480	516	538	553	571	596
Bauxite	327	353	377	384	384	384	384
Alumina	114	118	122	124	128	131	135
Diamonds and Gold	7	4	11	21	26	35	44
Coffee	1	1	1	2	5	11	21
Other	4	5	6	7	8	10	12

Source: World Bank

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Annex VIII

INITIAL ENVIRONMENTAL EXAMINATION OR CATEGORICAL EXCLUSION

Country:	Republic of Guinea
Title of Activity:	Guinea Economic Policy Reform Program (675-0217)
Funding:	FY 1986 - $10 million
Period of Project:	
IEE Drafted by:	REDSO/WCA, Wandra Mitchell
Environmental Action Recommended:	Categorical Exclusion

Discussion: This activity meets the criteria for Categorical Exclusion in accordance with Section 216.2(c) of Regulation 16, and is therefore exempted from the need for further environmental review. A total of Nine Million Five Hundred Thousand Dollars ($9,500,000) represents a cash transfer to the Government of Guinea (GOG) in support of the Government's policy reforms aimed at eliminating subsidies and other devices used to provide government-owned and operated agricultural production units with an unfair competitive advantage over their private sector counterparts. The Grant also supports the GOG's initiatives to adopt comprehensive credit policies that encourage private investment and borrowing, and to adopt Tax, Customs, Investment and Commercial codes that encourage private sector development in all sectors of the Guinean economy. The balance of $500,000 will be used to finance evaluation of this Program and technical services to the GOG in support of the above-mentioned policy reforms. The use of grant funds is not tied to either financing specific commodities or for a specifically identifiable project or projects. The categorical exclusion from environmental procedures for education, technical assistance or training programs and for analyses studies, academic or research workshops and meetings is applicable here. See Section 216.2(c)(2)(i) and (iii). This activity also meets the criterion of Section 216.2(c)(2)(vi) which provides a categorical exclusion for contributions to national organizations by the United States which are not for the purpose of carrying out a specifically identifiable project or projects.

Concurrence: Mark Wenting
AAO/Guinea, Mark Wenting

Bureau Environmental Officer's Decision:

Approved: Bessie L. Boyd

Disapproved: ____________________

Date: May 16, 1986
Bessie L. Boyd, AFR/TR/SDP

Clearance: GC/AFR: ________ Date: ____________________
Anthony Vance

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IKF/FBC

PRESIDENCE DE LA REPUBLIQUE

MINISTERE DU PLAN
ET DE LA
COOPÉRATION INTERNATIONALE

N° 805 /MPCI/CAB/DGCI/86

Objet :

ANNEX IX.

REPUBLIQUE DE GUINÉE
Travail-Justice-Solidarité

Conakry le 16 mai 1986

Le Ministre

A MONSIEUR LE DIRECTEUR
USAID/CONAKRY
Ambassade des Etats-Unis d'Amérique
CONAKRY

Monsieur le Directeur,

Suite aux nombreux entretiens entre le personnel de l'USAID et les différentes autorités guinéennes concernées, j'ai bien l'honneur de vous adresser la présente requête formelle pour un don de dix millions de dollars U.S. que votre Gouvernement a bien voulu offrir par le biais de l'Agence américaine pour le Développement International (USAID) comme soutien au programme de réformes économiques entrepris par mon Gouvernement et lancé par Son Excellence, le Président Lansana CONTE lors de son discours du 22 décembre 1985. Ces réformes ont notamment pour objectif la libéralisation de l'économie en favorisant la croissance et le développement du secteur privé. L'assistance offerte par votre Gouvernement appuiera cet effort de restaurer le secteur privé en Guinée afin qu'il puisse jouer un rôle moteur dans le développement économique tel que désiré par mon Gouvernement.

Au cours de ces derniers mois, les discussions techniques au sujet de l'utilisation de cette somme ont abouti à l'élaboration d'un programme qui vise à aider à résoudre les problèmes causés par le manque de devises, d'accès au crédit et de disponibilité de crédit pour le secteur privé. Les dollars fournis selon cet accord de subvention seront déboursés par le biais d'un système de ventes aux enchères hebdomadaires déjà mis en place par la Banque Centrale. La monnaie locale générée par

... / ...

la vente des dollars sera utilisée pour établir au sein des banques commerciales un système de crédit aux entreprises privées. Par conséquent, l'assistance offerte par le Gouvernement américain servira non seulement à alléger le déficit de notre balance de paiement mais aussi nous aidera à inaugurer une nouvelle politique de crédit et un système de crédit au service des entrepreneurs privés.

Mon Gouvernement est conscient qu'il pourrait s'avérer nécessaire d'utiliser jusqu'à 300.000 Dollars U.S. de cette subvention pour l'exécution, l'évaluation et le suivi de ce programme.

En conséquence, il est entendu qu'un accord séparé sera préparé pour une somme qui ne dépassera pas ce montant pour engager l'assistance technique nécessaire au bon déroulement de cet important programme.

Permettez-moi, Monsieur le Directeur, de saisir cette occasion pour vous exprimer les remerciements de mon Gouvernement pour le soutien du Gouvernement américain à notre effort de redressement national en général et particulièrement dans le cadre de cette nouvelle assistance pour un programme de réformes économiques.

Veuillez agréer, Monsieur le Directeur, l'expression de ma parfaite considération.

R.G.-Ministère du Plan et de la Coopération ... Le Ministre

EDOUARD BENJAMIN

ANNEX 10

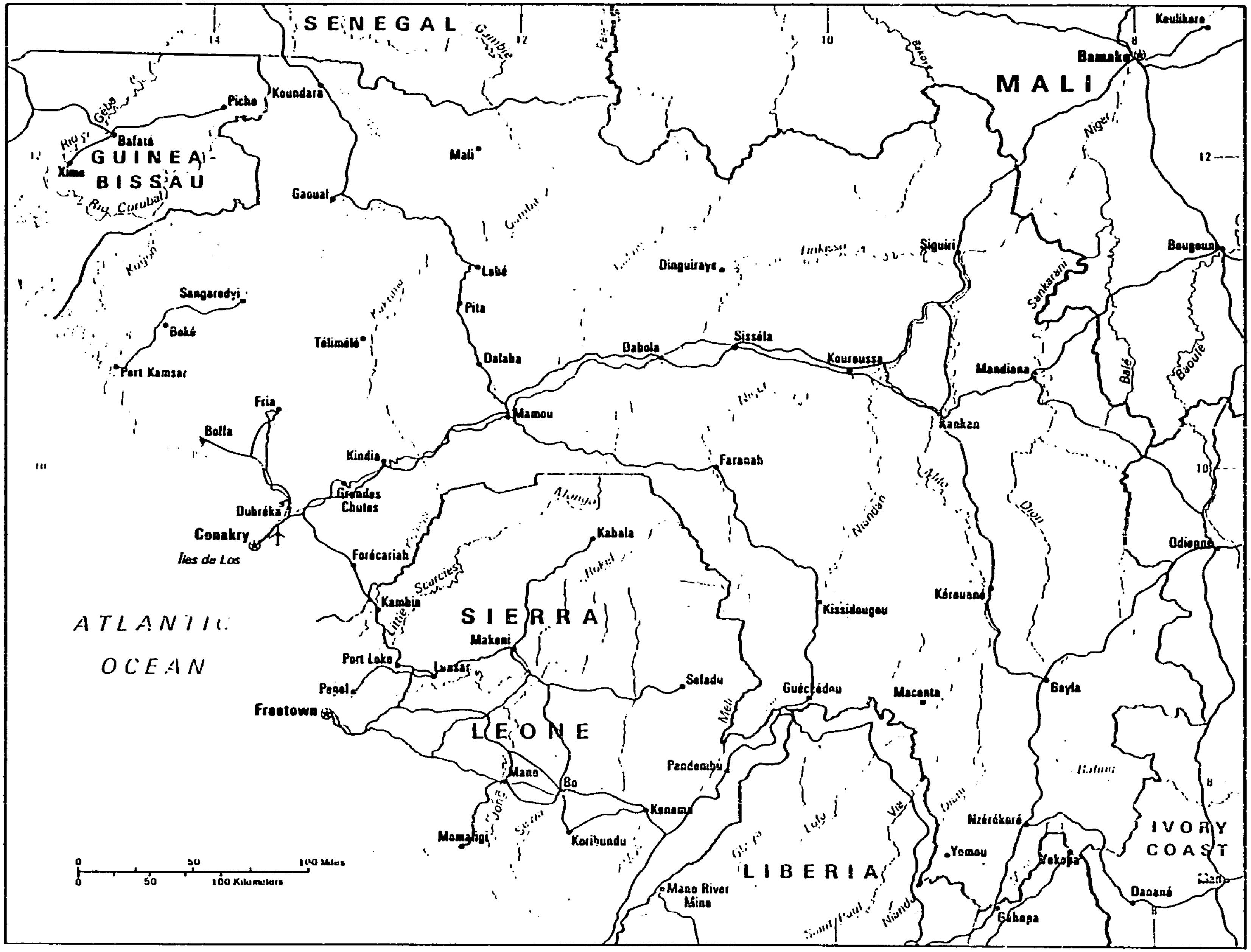
GUINEA: KEY ECONOMIC INDICATORS

Area: 95,000 square miles
Population: 5.9 million
Population Growth Rate: 2.8 percent
Exchange Rate: US$ 1.00 = 300 GF (public sector and mining activity)
US$ 1.00 = 340 GF (private sector)

Guinea[1]	1982	1983	1984	% Change Between 1983/84
National Accounts (Million of US$)				
GDP (at market prices)	1500	1520	1546	1.7
of which: Agriculture	42%	42%	42%	0
Industry & Mining	23%	23%	23%	0
Services	35%	35%	35%	0
Nominal GDP Per Capita (US dollars)	295	300	300	0
Balance of Payments (millions of US$)				
Trade Balance	64	123	99	-19
Exports	444	503	527	5
Imports	-380	-380	-428	13
Exports to US	121.1	105	220	5
Imports from US	-27.6	-22.1	-33.2	49
Services & Private Transfers (net)	-124	-140	-140	0
Official Transfers (net)	26	18	19	0
Balance on Current Account	-34	1	-22	-2300
External Debt (millions of US$)	1375	1500	1570	5
Mineral Production (millions of Metric tons)				
Bauxite	10.6	10.8	12.2	13
CBG	8.2	8.5	9.1	7
OBK	2.4	2.3	3.1	35
Alumina	.53	.57	.51	-10
Friguia	.53	.57	.51	-10
Diamonds (carats)	32,700	40,500	48,000	18
of which: Aredor (90% gem quality)			25,600	

[1] Data for Guinea have been collected from the Guinean Government, International Monetary Fund, World Bank, and Embassy estimates. All data have a relatively high margin of error and should be viewed as indicators of underlying trends.

Guinea



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Lambert Conformal Projection
Standard parallels 8° and 32°
Scale 1:4,000,000

Railroad
Road
Airport