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**MEMORANDUM AND RECOMMENDATION
OF THE
PRESIDENT OF THE
INTERNATIONAL DEVELOPMENT ASSOCIATION
TO THE
EXECUTIVE DIRECTORS
ON A
PROPOSED CREDIT OF SDR 26.2 MILLION (US\$35 MILLION EQUIVALENT)
TO
THE REPUBLIC OF BURUNDI
FOR AN
EMERGENCY ECONOMIC RECOVERY CREDIT**

March 23, 2000

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CURRENCY EQUIVALENTS

Currency Unit	Burundi Franc (FBu)
US\$1.00	FBu 570.0 (average for 1999)
SDR 1	US\$1.375

SYSTEM OF WEIGHT AND MEASURES

Metric

FISCAL YEAR

January 1 - December 31

ABBREVIATIONS

ABURTIP	Agence Burundaise des Travaux d'Intérêt Public
AfDB	African Development Bank
AGETIP	Agence d'Exécution des Travaux d'Intérêt Public
BRB	Banque de la République du Burundi (central bank)
BURSAP II	Burundi Social Action Project II
CAS	Country Assistance Strategy
CWIQ	Core Welfare Indicators Questionnaire
EAP	Emergency Assistance Project
ERC	Emergency Recovery Credit
EU	European Union
GDP	Gross Domestic Product
GNP	Gross National Product
IDA	International Development Association
IMF	International Monetary Fund
LCA	Local Currency Account
NGO	Non Governmental Organization
OAU	Organization of African Unity
OCHA	Office for the Coordination of Humanitarian Affairs (United Nations)
SA	Special Account
SME	Small or medium enterprise
UN	United Nations
UNDP	United Nations Development Programme

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REPUBLIC OF BURUNDI
EMERGENCY ECONOMIC RECOVERY CREDIT
CREDIT AND PROGRAM SUMMARY

Borrower: Republic of Burundi
Implementing Agency: Ministry of Finance
Credit Amount: SDR 26.2 million (US\$35 million equivalent)
Terms: Standard IDA with 40 years maturity
Economic Rate of Return: Not applicable
Poverty Rating: Not applicable
Environmental Rating: C

There is no separate Project Appraisal Document. A Technical Annex is being distributed together with this report. A technical proposal prepared by the Government of Burundi in consultation with IDA forms part of the Local Currency Account Manual and is appended to the Technical Annex .

Program Financing Plan	
IDA Emergency Economic Recovery Credit	Amount (US \$ millions)
IDA Emergency Economic Recovery Credit	35.0
Ongoing IDA Credits	25.5
Other donors	115.0
Total	97.5

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**MEMORANDUM AND RECOMMENDATION
OF THE PRESIDENT OF THE
INTERNATIONAL DEVELOPMENT ASSOCIATION
TO THE EXECUTIVE DIRECTORS ON A
PROPOSED EMERGENCY ECONOMIC RECOVERY CREDIT
TO THE REPUBLIC OF BURUNDI**

1. This memorandum seeks approval to extend an emergency economic recovery credit (EERC) for US\$35 million to the Republic of Burundi. This operation will help stabilize the economy, prepare an environment for economic recovery and restore essential social services to facilitate and support the ongoing negotiations for peace and reconciliation. The proceeds of the credit will provide quick-disbursing support to help stabilize the economy by alleviating the shortage of foreign exchange to the private sector that has reduced its ability to import and to finance the foreign exchange costs of exporting. Counterpart funds from the credit will help restore and operate basic essential services to minimal levels in public health, education, agriculture and village infrastructure. They will also help to inject liquidity into the private sector by reducing government arrears to its domestic suppliers.

Country Background

2. Burundi has known repeated ethnic violence since independence in 1962, with massacres occurring in 1965, 1972, 1988, 1991 and 1993. Economic sanctions imposed by regional leaders from 1996 through early 1999 in response to a coup d'état had a dramatic effect on growth, poverty, malnutrition and social indicators. The strife and sanctions have had a particularly severe social impact on the poor. The incidence of rural poverty has increased by 80 percent since 1993; that of urban poverty has doubled. GNP per capita fell from over US\$200 to US\$140 during the 1990s. National security is also affected by cross-border effects of the long decline of State authority in neighboring Democratic Republic of Congo (DRC) and the recent conflict in the eastern regions of DRC.

3. Social indicators have deteriorated following the crisis. In the five years following 1993, child immunization coverage declined from 83 percent to 54 percent, infant mortality increased from 110 per thousand live births to 136, malnutrition increased from 6 percent of children under five to 20 percent, and cases of major endemic diseases increased by over 200 percent. HIV prevalence is rising rapidly (21 percent in urban areas, 15 percent in rural areas). Forty thousand children have been orphaned by AIDS. Primary school enrollment has plummeted from 70 percent in 1993 to 44 percent at present, with a nadir of 9 percent in one area heavily stricken by violence. In mid-1999 there were still 550,000 internally displaced persons in over 300 sites; OCHA estimates that 91 percent of the displaced lack access to the daily minimum requirement of drinking water. In many villages, schools, health clinics, and other social services have been destroyed or damaged, qualified personnel have withdrawn to urban areas, and public expenditures in the education and health ministries have been reduced to salary payments.

4. Deteriorating security and the government's inability to restore peace, and donor observance of the regional economic sanctions contributed to the withdrawal of most bilateral and some multilateral aid. Most of the aid which remained was restricted to humanitarian objectives.

5. Progress is being made in political reconciliation and in establishing security. Internally, a transition constitution has been promulgated under which a coalition transition government has been established and the National Assembly broadened to 121 members to include minor political parties and representatives of civil society. Externally, negotiations involving 18 political parties (with two others admitted in March 2000), Government and the National Assembly are reportedly advancing in Arusha, Tanzania. The people of Burundi are actively pursuing reconciliation at the community level.

Bank Strategy and Donor Support

6. In light of the ongoing peace process, the worsening poverty and the emergency, the Bank prepared an *Interim Strategy* (Report 19592-BU, August 1999) to guide actions over the next 24 months. The Interim Strategy constructs an integrated framework for donors to address rising poverty, taking into consideration the underlying factors and proximate causes of conflict in Burundi and the triggers leading to repeated violence. It proposes a path to prepare for economic stabilization which also supports the peace process. It seeks to : (1) promote governance and ownership of reconciliation and reconstruction through a participatory approach to rehabilitating social infrastructure damaged or destroyed by the conflict; (2) create productive employment, boost purchasing power and give a broad segment of the population an economic stake in reconciliation while providing a vehicle for the eventual reintegration of demobilized combatants; and (3) restore key imports and essential social services to facilitate private sector recovery and operate the rehabilitated infrastructure in health, education, agriculture and return of displaced households. The proposed EERC is one of three immediate operations under the Interim Strategy.

7. The UNDP and the Government are preparing a Round Table for this year which is expected to draw in part from the Bank's strategy. In general, however, bilateral donors are awaiting the launching of the PER to determine the configuration for fuller development assistance.

8. The European Union is on course to provide a package amounting to up to Euro 85 million, of which the EC may seek member notification for immediate release of Euro 30 million as blocked reserves and Euro 7 million as balance of payments support to prevent economic collapse. Funds targeting the poor and vulnerable as part of a Euro 48 million assistance program awaits the preliminary results of the PER and would be made available as budget support in line with implementation of recommendations of the PER.

9. Burundi has acquitted itself of its obligations to the IMF. With the ending of the regional economic embargo the Fund has begun to normalize its relations with the country. It delayed its submission of 1999 Article IV consultations to its Board to parallel design of the EERC; the discussions were held on March 15, 2000 and a mission to discuss *Emergency Post-Conflict Assistance* of SDR 19.3 million (US\$25.8 million) awaits only the official invitation of the Government which is being processed. The aim is to provide this assistance to coincide with the effectiveness of the EERC.

10. Belgium is considering US\$2 million in co-finance for the EERC from funds already on deposit with the Bank for cofinancing project activities. France is rebuilding its aid program beginning with a line of credit to SMEs. Subject to Burundi stabilizing its bilateral debt arrears, France intends to co-finance BURSAP II and complement planned Bank activities within the

interim strategy. The AfDB is considering new assistance projects that will support the second, employment generation leg of the Interim Strategy. AfDB has authorized a project for hospital rehabilitation, and plans support for the Ministry of Public Health. Finally, the AfDB met with the Burundian authorities in March to discuss co-financing support linked to the EERC now under preparation and which is currently expected in June.

Project Objectives and Benefits

11. The Credit is intended to support the stabilization and recovery of the private sector and finance public expenditures for rehabilitation in health, education, agriculture, infrastructure, and reinsertion of households stricken by conflict. In parallel with the implementation of the Credit, - the Government intends to do a Public Expenditure Review which would provide the transparency sought by other donors to resume significant levels of development assistance. At the end of one year the EERC would have helped to stabilize the macro-economy and facilitate the success of complementary economic recovery measures by providing foreign exchange to support macroeconomic balance. The policy reforms and complementary activities associated with the EERC are expected to improve macroeconomic performance as compared to how it would be in the absence of assistance, permitting legislative oversight and making government activities more transparent.

Risks

12. There is a risk that Burundi will return to widespread violence, as has happened repeatedly in the past. Reconciliation depends upon peace processes outside Bank control. However, the full range of significant donor assistance is implicitly conditioned on progress toward reconciliation. This provides an incentive for compliance with the agreements made in parallel to the EERC.

13. Donors are concerned that any budget support, without appropriate controls, might be misused for military purposes, or may weaken incentives for incumbents within the government to negotiate with others on an equal basis. It is for this reason the EERC differs from normal Bank "quick-disbursing" operations. Foreign exchange will be provided to the private sector, its distribution and value determined through auction. This credit will also follow the practice used elsewhere of looking at the increase in social and development expenditure which would not be possible without assistance. The PER will provide a basis for monitoring budget execution.

14. There is a risk that providing foreign exchange will not elicit a private sector response: much of the sector's working capital is tied up in government arrears and an illiquid banking system is unable to provide credit, while the injection of liquidity when the Government clears its arrears will follow rather than precede the foreign exchange auction. To mitigate this risk, the liquidity provided by the first round of auction of the SA proceeds and government arrears clearance will facilitate the second and subsequent auctions. In the event that this does not lead to a competitive auction, a fallback position would provide direct payments to foreign suppliers and creditors from the Special Account with reimbursement at the "second market" (indicative competitive) rate.

15. Corruption and issues dealing with transparency are important and must be monitored closely. Capacity building supported by donors and financiers, and support to the judicial system

being provided by other donors, are important steps in this regard. The Government has requested assistance to its anti-corruption program from other donors and may request an IDF grant.

16. A broader risk is that extremists may pursue a strategy of intimidation of all involved, including the local population and the international community. The monitoring procedures assure that poor and marginal populations receive increases in social sector expenditures. Strengthening the role of the State will reduce the risk from certain groups who may continue to use violence to destabilize society for ideological reasons.

17. If donor response is inadequate or delayed, the crisis may lead to a situation in which it will be extremely difficult and costly to provide the resources to stabilize and restore the economy. The people of Burundi are actively seeking peace and reconciliation, but further deterioration in the economic and financial situation threatens this process. As well, the emergency may have regional implications in an already difficult environment. The proposed credit aims to mitigate the impact of the emergency on private sector activities and to support Burundi's efforts to reconcile and eventually focus on peaceful economic development.

Recommendation

18. I am satisfied that the proposed Credit will be effective in these purposes and would comply with the Articles of Agreement of the Association and recommend that the Executive Directors approve it.

James D. Wolfensohn
President

By Shengman Zhang

Washington, D.C.
March 23, 2000