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Press Information Notices

January–April 1998 • No. 1

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January–April 1998 • No. 1

International Monetary Fund
Washington, DC

ISBN 1-55775-754-2 • ISSN 1020-6779

This new series of IMF Economic Reviews, registered as ISSN 1020-6779, replaces a former series of the same name, registered as ISSN 1020-0576. The former series has been discontinued.

The following symbols have been used throughout this series:

na	to indicate not applicable;
. . .	to indicate that data are not available;
—	to indicate that the figure is zero or less than half the final digit shown, or that the item does not exist;
–	between years or months (e.g., 1997–98 or January–June) to indicate the years or months covered, including the beginning and ending years or months;
/	between years (e.g., 1997/98) to indicate a crop or fiscal (financial) year.

"Billion" means a thousand million.

Minor discrepancies between constituent figures and totals are due to rounding.

The term "country," as used in this series, does not in all cases refer to a territorial entity that is a state as understood by international law and practice; the term also covers some territorial entities that are not states, but for which statistical data are maintained and provided internationally on a separate and independent basis.

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About This Series

This volume is the first of a new series, *IMF Economic Reviews*, intended to make available on a more timely basis the Executive Board reviews of member economies previously released in the *Annual Report*. It is also intended to supplement the electronic availability of such assessments on the IMF's web site.

In carrying out its responsibility for overseeing the international monetary system and ensuring surveillance over members' economic policies, the IMF holds bilateral consultations under Article IV of its Articles of Agreement with all its member countries, in most cases every year. As part of these consultations, an IMF staff team visits a country to discuss with officials economic developments and the monetary, fiscal, and structural policies that the authorities are following. On its return to IMF headquarters, the team prepares a report analyzing the economic situation and evaluating the stance of policies. That report is then discussed by the Executive Board. At the end of the discussion, the Chairman of the Board summarizes the views expressed by Executive Directors during the meeting. This summing up is transmitted to the country's authorities.

In April 1997, Directors agreed to issue, at the request of a member country, the Board's summing up, supplemented by a short account of significant macroeconomic and structural developments at the time of the consultation.These summaries, released by the IMF as "Press Information Notices," are posted on the IMF's Internet web site (http://www.imf.org). They are intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

In May 1998, the Board decided to have Press Information Notices compiled and published every four months. At the same time, the selection of Article IV consultation summaries was eliminated from the *1998 Annual Report*. The next two issues in the tri-annual *IMF Economic Reviews* series will publish all Press Information Notices released during May–August and September–December 1998.

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Press Information Notice (PIN) No. 98/9
FOR IMMEDIATE RELEASE
February 23, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Argentina

The IMF Executive Board on February 4, 1998 concluded the 1997 Article IV consultation[1] with Argentina.

Background

Argentina's robust recovery from the recession it experienced in 1995 and early 1996 continued in 1997 at a rapid pace, resulting in **real GDP** growth that is likely to have exceeded 8 percent for the year. Investment continued to drive growth, with output expanding strongly in energy, construction, the financial sector, and manufacturing. The economic recovery was accompanied by an improvement in the employment situation. The **unemployment** rate fell from 17.3 percent to 13.7 percent between October 1996 and October 1997 on the strength of a 7 percent job growth, while wages remained flat. Consumer price **inflation** remained near zero in 1997, while wholesale prices actually declined.

The **fiscal situation** improved significantly in 1997, despite ongoing transitional costs from the switchover to privately administered pension funds equivalent to some 1 percent of GDP a year The overall public sector deficit declined from 3.3 percent of GDP in 1996 to an estimated 1.9 percent in 1997, while the deficit of the federal government (including the costs associated with the reform of the civil service and the transfer to the federal level of certain provincial pension funds) fell from 2.2 percent of GDP to 1.4 percent. Federal government revenues rose by 0.8 percent of GDP, reflecting an increase in fuel taxes, higher revenues from corporate income taxes, and higher nontax revenue. Expenditures declined as a share of GDP, with civil

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service and social security reforms contributing to contain outlays and offsetting increases in public investment, transfers to provincial governments, and interest payments.

Since 1995, the Argentine **banking sector** has been strengthened considerably. The number of financial institutions declined by about 20 percent and foreign-owned banks greatly increased their presence in the country. The average capital adequacy ratio (according to Basle criteria) rose from 18 percent to 20 percent by mid-1997, and the share of nonperforming assets declined somewhat. Central bank reserves climbed by more than US$3 billion in 1997, reaching US$22.8 billion by year-end, while commercial banks held some US$7 billion in liquid assets abroad. In addition, a contingent repo facility was established with foreign banks to provide liquidity to the banking system, in an amount equivalent to some 10 percent of the system's deposits, in the event of a crisis. Interest rates fell significantly in the first half of 1997, before a temporary rebound in the wake of the Asian crisis.

High domestic demand along with a strong U.S. dollar and a weak harvest contributed to a substantial increase in the **external current account** deficit, which moved from 1.9 percent of GDP in 1996 to an estimated 3.8 percent of GDP in 1997. Underlying this deterioration was the decline in the trade balance from near equilibrium in 1996 to a deficit of US$4.9 billion (1.5 percent of GDP) in 1997. Imports rose by 27 percent, while exports rose by 6½ percent. Import growth was particularly strong in capital goods (37 percent), but consumer goods imports were also robust (up 27 percent). The current account deficit was more than covered by a strong increase in **capital inflows**. Foreign direct investment climbed by nearly 60 percent to US$6½ billion, financing more than half of the current account deficit. A strong inflow of deposits to the banking system and external borrowing (most of it long-term) covered the remainder of the deficit and permitted an accumulation of foreign exchange reserves.

The authorities made further progress in **structural reforms** in 1997, building on the achievements in privatization, social security reform, and public sector restructuring already made since 1991. The medical benefits program for retirees (PAMI) was strengthened, management of the public social security system was rationalized, and several deficient provincial pension funds were taken over by the central government and set on the road to recovery. As regards privatization, the postal services were leased to the private sector and a number of provincial banks and utilities were sold.

So far, Argentina has weathered well the world capital **market turbulence** of the latter part of 1997. Interest rates increased markedly in late October and November, but have since declined to near pre-crisis levels. Confidence in the financial system remained high; deposits in the banking system (both in U.S. dollars and in Argentine pesos) continued to climb, as did central bank foreign exchange reserves. Argentina has seen no interruption in its access to international capital markets, albeit this has come at a somewhat higher cost. Since November, the government has floated bonds of up to 30 year maturity in diversified markets for more than US$1.7 billion and secured syndicated bank financing of US$2 billion.

A three-year **extended arrangement with the IMF** was approved on February 4, 1998 (see Press Release 98/1), for a total of SDR 2,080 million (45 percent of the country's quota on an annual basis). This arrangement is in support of the authorities' program of further fiscal consolidation and a deepening of structural reforms. The authorities have indicated that they do

not intend to draw on this arrangement and will treat it as a "precautionary" arrangement to underpin their reform efforts. Under the program, the overall public sector deficit will be reduced to under ½ percent of GDP by 2000, with further reforms in taxation, fiscal relations with provincial governments, and the public social security system. A labor market reform will be implemented to boost job creation and competitiveness by improving wage and workplace flexibility. The government has undertaken to continue the privatization process—among other things, with the sale of the National Mortgage Bank (BHN) to be completed in 1998—and has announced its intention to privatize Banco de la Nación (the country's largest bank) later in the program period. Further financial sector reforms, including enhanced prudential regulations and steps to increase the efficiency and transparency of financial intermediation will be implemented The program also includes provisions for improvements in health care, poverty alleviation, the judicial system and public ethics, and education.

Executive Board Assessment

Executive Directors expressed satisfaction with the strong investment-led growth and continued absence of inflationary pressures in 1997. They welcomed the sharp drop in the rate of unemployment during the year, but noted that unemployment still remains at a relatively high level, reflecting continuing rigidities in the labor market. Directors commended the authorities for their macroeconomic and financial management during 1997, which had helped the country weather the recent turbulence in international financial markets. They noted that the continued growth of foreign exchange reserves and banking sector deposits, as well as the absence of public sector financing problems in late 1997, augured well for Argentina, but cautioned that external sector developments must be closely monitored.

Directors welcomed the authorities' desire to maintain a close dialogue with the IMF, and also welcomed the precautionary nature of the proposed extended arrangement. Some Directors observed that the proposed arrangement is especially important in view of the uncertainties induced by the current global market turbulence. In this environment, Directors attached importance to the authorities' commitment to take prompt action, if and as needed, to ensure achievement of the program targets, and welcomed the inclusion of special consultation clauses in the arrangement. They also welcomed the focus of the proposed program on key structural reforms.

Directors expressed satisfaction with the fiscal consolidation achieved during 1997, but underscored the importance of further fiscal adjustment. In view of the uncertainty surrounding the macroeconomic outlook and the prospective current account deficits, Directors stressed that the authorities need to stand ready to take further fiscal action should a revenue shortfall materialize, or should financing prove difficult in 1998. Directors welcomed the authorities' commitment to introduce by mid-1998 a comprehensive tax reform proposal, aimed at improving the efficiency and equity of the tax system, broadening the bases of the income tax and the value-added tax, and promoting the competitiveness of the economy. Directors noted that some progress had been made in 1997 in improving tax compliance, and encouraged the authorities to persevere with their efforts to strengthen the tax administration. Directors welcomed the authorities' intention to contain the overall growth of public spending, through better prioritization of expenditure programs and efforts to improve their transparency and efficiency. Several Directors also encouraged the authorities to undertake a comprehensive reform of

intergovernmental fiscal relations, which should help strengthen the provinces' own revenue-generating capacity.

Directors commended the authorities for the progress made so far in strengthening, and modernizing the domestic financial system. They noted the consolidation in the banking system, the strengthening of the banks' capital and liquid reserve position, and improvements in the quality of banking sector assets. Directors welcomed the authorities' plans to firm prudential regulation and supervision further, as well as to improve dissemination of financial market information. They expressed support for the government's announced intention to privatize Banco de la Nación, and noted the importance of the privatization of remaining provincial banks for strengthening the financial system and to improving allocative efficiency and fiscal discipline.

Directors noted the substantial progress already made by Argentina in recent years in structural reforms, particularly in privatization, pension reform, and in the rationalization of the state. They welcomed the authorities' intentions to continue structural reforms in key areas of the economy and society, and the focus on second generation reforms. In particular, they noted the importance of labor market reform in promoting a further reduction in unemployment and continued external competitiveness. They welcomed the authorities' commitment to secure the early passage of a labor market reform package to significantly enhance labor market flexibility, including a significant reduction in dismissal costs and a progressive elimination of the "ultra-actividad". Directors also welcomed the government's determination to press ahead with the proposed reforms of the judicial system to improve its efficiency, especially in areas of macroeconomic relevance.

Directors noted that the external current account deficit had increased substantially in 1997, and stressed the importance of preventing a further deterioration in 1998, and of ensuring a gradual improvement in subsequent years, especially in view of the still high level of the external debt service in relation to exports. They noted, in particular, the growing regional concentration of Argentina's exports, and encouraged efforts to diversify export markets. Therefore, Directors encouraged the authorities to closely monitor current account developments. They noted that, although Argentina has had no difficulty in obtaining needed external financing so far, it remains vulnerable to changes in external market conditions. Therefore, Directors welcomed the authorities' commitment to take quick and decisive action to restrain domestic demand, should the current account deteriorate further or prospects for external financing worsen. Several Directors urged the authorities to press within MERCOSUR for the early reversal of the recent increase in the common external tariff.

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Argentina: Selected Economic Indicators

	1993	1994	1995	1996	Est. 1997
Real economy (change in percent)					
Real GDP	6.3	8.5	-4.6	4.2	8.1
Domestic demand	7.6	9.8	-8.4	5.9	10.8
CPI (end of period)	6.8	3.9	1.6	0.0	0.3
Unemployment rate (October, in percent)	9.2	12.2	16.4	17.3	13.7
Gross national savings (percent of GDP)	15.3	16.3	16.5	15.7	16.2
Gross national investment (percent of GDP)	18.4	20.0	18.0	17.7	20.0
Public finance (percent of GDP)					
Federal government balance	0.9	-0.5	-1.4	-2.2	-1.4
Overall public sector balance	-0.2	-1.7	-3.4	-3.3	-1.9
Total public debt	29.2	31.1	35.9	37.4	36.2
Money and interest rates					
Net domestic credit (change in percent)	21.0	19.1	5.7	4.0	13.1
Private sector deposits (change in percent)	54.1	19.7	-3.1	22.2	28.1
Interest rates (average, in percent per annum)					
90-day peso time deposits	12.8	8.8	13.1	7.3	7.0
30-day peso prime rate	12.3	10.1	17.8	10.5	9.1
Balance of Payments (in millions of US$)					
Trade balance	-2,427	-5,750	844	49	-4,892
Exports (f.o.b.)	13,117	15,841	20,967	23,811	25,360
Imports (c.i.f.)	-15,544	-21,591	-20,123	-23,762	-30,252
Current account 1/	-7,853	-10,341	-4,302	-5,781	-12,196
As percent of GDP	-3.0	-3.7	-1.5	-1.9	-3.8
External debt (percent of GDP)	23.4	24.7	24.4	25.9	26.3

Sources: Central Reserve Bank of Argentina, National Institute of Statistics, FIEL; and IMFstaff estimates.

1/ The authorities estimate a lower current account deficit (by about US$1.6 billion or 0.5 percent of GDP) on account of interests receipts imputed on assets held abroad by the private sector. Work on improving the estimation of these assets is underway.

Press Information Notice (PIN) No. 98/17
FOR IMMEDIATE RELEASE
March 12, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Armenia

The IMF Executive Board on February 6, 1998 concluded the 1997 Article IV consultation[1] with Armenia, and completed the mid-term review under the second annual arrangement under the Enhanced Structural Adjustment Facility (ESAF).

Background

In December 1994, Armenia embarked on a comprehensive program of macroeconomic stabilization and structural reform with the financial support of international financial institutions and donors. By end-1996, the firm implementation of these policies had contributed to the reduction of inflation to single digit levels and to the resumption of output growth at an annual rate of about 6 percent. Prices were liberalized, with the exception of those for public utilities, communal services, and urban transport which, nonetheless, were adjusted several times. Privatization of small and medium enterprises proceeded as targeted, and decisive steps were taken to reform various sectors, including banking, education and health. During this period, the IMF provided financial support for Armenia's program under the Systemic Transformation Facility (December 1994), a one-year stand-by (June 1995), and a three-year ESAF (February 1996).

Armenia's record of good macroeconomic performance suffered a setback that started in the third quarter of 1996 and lasted well into the first half of 1997. For 1997 as a whole, real GDP growth slowed to 3 percent, inflation accelerated to almost 22 percent, and the external current account deficit (excluding official transfers) stalled at around 27 percent of GDP. Although real shocks affected agricultural output in mid-1997, there was some easing of financial policies as

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well as a loss in the momentum of structural reform.

The deficit of the state budget (on an accrual basis) is estimated to have reached 6.3 percent of GDP in 1997, down from 8.6 percent in 1996. Tax revenue performance was strong and expenditures were kept slightly below the level of the preceding year. However, the government incurred expenditure arrears in the first three quarters of 1997, and engaged in sizable quasi-fiscal operations via the extension of guarantees on bank borrowing by major enterprises. There was further progress in improving the functioning of the treasury, the targeting of the social safety net, and the pension system.

Reserve and broad money continued to grow strongly, albeit at a lower rate than in the previous year. Reserve money growth was led by increases in domestic credit during the first half of 1997. Thereafter, it was fueled by large capital inflows, which could not be sterilized given the limited instruments of monetary control. Following a 14 percent depreciation in the first 7 months, the exchange rate remained at around dram 500 per U.S. dollar until the end of the year.

Armenia's external current account and trade deficits did not improve as expected in 1997, mainly on account of a sharp increase in recorded imports (particularly shuttle trade) driven in part by the rapid expansion in domestic credit. Exports are estimated to have been significantly lower than in 1996. Official and private transfers remained sizable. The management of the external debt improved further. Armenia concluded debt restructuring agreements with Russia and Turkmenistan, and made debt service payments to the European Union.

There has been a noticeable improvement in the overall health of the banking system, as evidenced by a sharp decline in the extent of nonperforming loans. Significant progress has also been achieved in the area of privatization. In late 1997, the authorities initiated the privatization of 11 large enterprises through international tenders, but interest by prospective buyers has been mixed. In December 1997, the government approved a financial rehabilitation plan for the energy sector and a program to privatize energy enterprises.

Following on the steps taken in the fourth quarter of 1997 to restore macroeconomic stability, the authorities have designed a package of corrective policies for 1998. Inflation is expected to decline to 9 percent at end-1998 and the external current account (excluding official transfers) to 22 percent of GDP. Building on an acceleration of structural reform, real GDP growth is expected to recover to over 5 percent in 1998. Consistent with continued financial restraint, the Armenian Parliament approved the 1998 budget which calls for a state budget deficit of 5.5 percent of GDP, and the Central Bank of Armenia has announced a tight monetary program. Important financial sector reforms, particularly as regards enhanced bank supervision, will continue. Privatization of small and medium-size enterprises is expected to surge with the introduction of cash privatization, and efforts to attract foreign investors to the international tenders will be increased. The government also intends to embark on a civil service reform and will seek to obtain membership with the World Trade Organization in 1998.

Executive Board Assessment

Recalling Armenia's good track record of macroeconomic performance and structural reforms, Directors expressed concern at the setbacks in 1997. While noting the negative effects of real shocks on macroeconomic performance, Directors regretted the more-expansionary-than-programmed macroeconomic policy stance, and the loss of momentum in structural reforms. Accordingly, they warmly welcomed the recent efforts to put the program back on track, notably the tightening of macroeconomic policies and the steps taken to accelerate and deepen the structural reform process, which were already beginning to produce some positive results. In this regard, while noting the uncertainty created by the recent resignation of some senior officials, Directors were encouraged by the authorities' reaffirmation of their continuing commitment to the IMF-supported program. They underscored the fact that major issues remained to be addressed, particularly with regard to fiscal policy, privatization, the financial rehabilitation of the energy sector, and external debt management, in order to improve the environment for increased investment and to build a lasting basis for sustained growth.

Directors stressed the importance of maintaining a prudent fiscal policy stance and improving fiscal management. They welcomed the strong revenue performance in the second half of 1997, which had allowed the clearing of expenditure arrears. In this regard, Directors noted the authorities' efforts to improve tax administration, broaden the tax base, and enforce payments discipline—although further efforts would be needed, especially to address the problem of tax arrears. While noting the authorities' efforts to improve the management of the treasury, Directors expressed concern about the recurrent problems in controlling budgetary expenditure and the recourse to expenditure sequestration. In this regard, further progress should be achieved through the firm implementation of the specific action plans that incorporated the technical advice given by IMF-led teams of experts. Directors also welcomed the adoption of new procedures on accounting and financing of budgetary expenditures aimed at avoiding the reemergence of expenditure arrears. They welcomed the initiative to rationalize and improve the targeting of the social safety net, and to strengthen the pension system, so as to protect the most vulnerable groups in society.

Directors commended the authorities' recent implementation of a tighter monetary program and their decision to cease the government's net borrowing from the central bank in 1998. They welcomed the securitization of the outstanding central bank claims on the government, which would improve monetary management, and help to deepen and broaden financial markets. Directors also welcomed the government's decree to cease providing guarantees on domestic commercial borrowing by state enterprises, a step that would help moderate such credit expansion. They considered appropriate the government's intention to pursue a foreign exchange policy that will allow the exchange rate to reflect underlying market pressures.

Directors expressed concern about the weakening of the external current account and the sensitivity of the trade balance to unanticipated changes in import prices. The vulnerability of the external sector underscored the importance of closely monitoring trade developments and adopting a cautious approach to external borrowing. Noting that Armenia would continue to depend on concessional foreign assistance for the foreseeable future, they supported the

authorities' efforts to monitor external borrowing more closely. Directors called for stringent efforts over the coming years to curtail the accumulation of nonconcessional debt.

Directors noted that, although some structural elements of the program had fallen behind schedule, positive actions had been taken, particularly in the area of privatization. They endorsed the introduction of a cash privatization program in 1998, which should help reestablish the momentum of privatization of small- and medium-sized enterprises, and enhance the scope for foreign participation in the privatization of large enterprises. They emphasized the importance of designing a comprehensive strategy for the use of the one-time proceeds arising from such privatization, and welcomed the authorities' commitment to limit the use of these proceeds for budgetary support and to improve the profile of debt.

Directors welcomed the progress that had been made in strengthening the banking system, particularly in the areas of banking supervision, improved loan portfolios, and the move to international accounting standards. The decision to place two banks under special supervision in 1997 had been noteworthy. While Directors noted the government's decision to intervene in the third problematical bank, they stressed that it was important to signal that such an intervention was exceptional and temporary.

Directors welcomed the financial rehabilitation plan for the energy sector, and stressed the importance of developing an appropriate strategy for the major energy-consuming enterprises as soon as possible, so as to limit the government's financial involvement in them in the future. In this regard, Directors supported the authorities' intention to explore avenues to reduce the cost of financing for completion of the thermal plant, which would eventually replace the nuclear power plant, and encouraged other creditors to help find a creative solution to this problem.

Directors welcomed the significant progress that had been made in improving the quality, coverage, and timeliness of macroeconomic data, and encouraged the authorities to adopt an even more open policy on data dissemination.

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Armenia: Selected Economic Indicators

	1994	1995	1996	1997 1/
Output				
GDP (billions of dram)	187	522	660	778
Real GDP growth (percent change) 2/	5.4	6.9	5.8	3.3
GDP in millions of U.S. dollars 3/	651	1,286	1,594	1,585
CPI Inflation (in percent)				
Period average 4/	5,273	176.7	18.7	14.0
End-period 4/	1,885	31.9	5.8	21.8
Exchange rates (drams/US$)				
Period average 4/	287	406	414	491
End-period 4/	406	402	435	495
State budget operations (in percent of GDP) 5/				
Total revenue and grants 4/	26.1	17.8	15.1	16.8
of which tax revenue 4/	11.5	10.7	10.7	13.6
Total expenditure and net lending 4/	42.9	27.3	23.7	23.1
State budget balance (accrual; deficit '-') 4/	-16.8	-9.6	-8.6	-6.3
State budget balance (cash; deficit '-') 4/	-10.5	-11.7	-9.3	-6.3
Monetary Sector				
Reserve money (end of period growth rate, in percent) 4/	833.2	97.9	40.5	22.5
Broad money (end of period growth rate, in percent) 4/	684.2	68.7	35.1	29.1
Velocity 6/	4.8	3.7	3.4	3.1
Dram broad money (end of period growth rate, in percent) 4/	726.9	129.9	34.1	8.6
Dram velocity 6/	8.2	4.6	4.4	4.7
External Sector				
Current account balance (millions of U.S. dollars) 7/	-231	-483	-424	-428
Total external debt (millions of U.S. dollars)	200	371	614	798
External debt service (in percent of exports of G&NFS)				
On amounts due	3.0	20.6	18.7	22.0
On amounts paid	12.3	4.2	12.4	15.1
Gross international reserves				
In months of imports of goods & non-factor services	0.7	1.6	2.2	2.8

Sources: Armenian authorities; and IMF staff.

1/ Estimated unless otherwise indicated.
2/ Over same period of previous year.
3/ Calculated on the basis of the average exchange rate.
4/ 1997 data shown are actual.
5/ Includes the republican and local budgets.
6/ In final quarter of the period using GDP of the corresponding quarter, seasonally adjusted.
7/ Excludes official transfers.

Press Information Notice (PIN) No. 98/22
FOR IMMEDIATE RELEASE
March 31, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with The Bahamas

The IMF Executive Board on March 13, 1998 concluded the 1997 Article IV consultation[1] with The Bahamas.

Background

Since 1995, the Bahamian economy has experienced a marked recovery based on prudent financial policies, stepped up private investment—mainly in the tourism and shipping sectors—and continued growth in financial and other services. **Real GDP** growth went up from less than 1 percent a year in 1994–95 to around 4 percent in 1996 as increased hotel capacity and the pickup in consumer demand in the United States led to higher tourist expenditure. The recovery was also boosted by foreign investment in a large ship repair and transshipment terminal, steady growth in financial services, and a pickup in residential construction. The pace of the recovery is estimated to have moderated to about 3 percent in 1997 as a reduction in hotel capacity due to ongoing construction and refurbishment led to a slowdown in the growth of tourist expenditure. In line with the increase in economic activity, the **unemployment** rate declined from more than 13 percent in 1993–94 to less than 10 percent in 1997. **Inflation** remains in the low single digits, reflecting the fixed parity of the currency with the U.S. dollar, the openness of the economy, and cautious financial policies. The rate of price increase declined from 1.1 percent during 1996 to less than 1 percent during 1997.

The overall position of the **nonfinancial public sector** shifted from near balance in 1995 to a deficit of 1.4 percent of GDP in 1996 mainly because of higher spending on infrastructure projects. Spending on infrastructure continued to increase in 1997, and indicators point to a further widening in the overall deficit to over 3 percent of GDP in that year. The deficits in

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1996–97 were financed mainly through the issue of bonds to the domestic private sector.

Liquidity in the **banking system** remained largely unchanged in the twelve months ended September 1997 as the growth in private sector deposits was matched by credit expansion to the private sector. During this period there was little movement in interest rates on commercial bank deposits and loans, and the treasury bill rate fell slightly to 4.2 percent. The authorities have engaged in open market operations to maintain credit conditions consistent with maintenance of the fixed exchange rate peg with the U.S. dollar. In the area of bank supervision, the authorities' recent efforts have focused on ensuring compliance with the prudential and accounting standards established by the Base Committee; they have also taken steps to establish a deposit insurance scheme.

The **external current account** deficit widened from 4 percent of GDP in 1995 to about 9 percent in 1997 as imports related to the construction of tourist facilities rose sharply. The deficit was financed mainly by private, long-term capital inflows, the international reserves of the central bank increased from US$163 million in December 1996 to US$218 million in December 1997. At end-1997 the stock of public sector external debt stood at 8.5 percent of GDP, and the ratio of public sector debt service to exports of goods and services at 5.5 percent.

The authorities have made progress in the area of **structural reform.** Regarding privatization, all but one of the major hotels have been sold, the government has reduced further its holdings in a commercial bank, and the partial divestment of the telecommunications company is proceeding. In the financial sector, a legal framework for the operation of trusts and mutual funds has been established, legislation authorizing the establishment of a stock market as well as a regulatory framework for the securities industry is expected to be approved shortly, and work has been initiated on updating regulations for pension schemes and insurance companies. Legislation was enacted in December 1996 aimed at making it a crime to launder the proceeds of any criminal activity, and the authorities intend to adopt the disclosure standards of The Offshore Group of Banking Supervisors, which call for banks to provide information on the use of funds when there is reasonable suspicion of criminal activity.

Executive Board Assessment

Executive Directors commended the authorities for the pursuit of sound macroeconomic policies that had been successful in preserving price stability, increasing investor confidence, and attracting significant flows of private investment. As a result of these policies, real GDP growth had picked up and is now more broad based, inflation remained low, unemployment continued to decline, and social indicators remained favorable.

Directors observed that sustaining the recovery over the medium term would require maintaining prudent financial policies. They noted that the restrained fiscal stance of earlier years had given way to a weakening of the government finances in Fiscal Year 1996/97, and they stressed the importance of restoring a tight fiscal stance.

Noting the lack of buoyancy in revenues in recent years, Directors welcomed the ongoing review of revenue performance. They pointed out that it was essential to broaden the tax base by reducing tax concessions and exemptions and to strengthen tax administration. On the expenditure side, Directors recommended containing the size of the wage bill and outlays on goods and services through phasing out the current system of uniform across-the-board pay increases and placing greater reliance on performance-based pay.

Directors stressed that wage restraint in the public sector, supported by improved education and training to increase labor skills, and greater flexibility in labor arrangements, would help maintain competitiveness in tourism and other sectors over the medium term.

Directors welcomed the authorities' commitment to pursue a monetary policy consistent with the fixed exchange regime, which they considered is serving the authorities well. Directors commended the authorities for their efforts to meet international standards of bank supervision and their prompt and effective response to the recent failure of a small domestic bank. They urged that the planned review of supervisory practices be carried out promptly, and that the capacity for the on-site inspection of banks be developed.

Directors noted that the large external current account deficit in 1997 was financed mainly by direct investment and other long-term private capital inflows, and urged the authorities to monitor external developments carefully.

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THE BAHAMAS: Selected Economic Indicators

	1994	1995	1996	Prel. 1997
	(Annual percentage changes, unless otherwise indicated)			
Domestic economy				
Real GDP 1/	0.9	0.3	4.2	3.0
Number of stopover visitor days 2/	2.5	2.3	4.7	-0.4
Consumer price index (12-month increase)	1.5	1.7	1.1	0.8
Unemployment rate (in percent of labor force)	13.3	10.9	11.5	9.8
	(In percent of GDP at market prices)			
Financial variables				
Nonfinancial public sector overall balance	0.5	-0.2	-1.4	-3.8
Nonfinancial public sector savings	2.9	2.4	2.6	2.6
Central government overall balance	-1.0	-0.9	-1.5	-3.9
Change in broad money (in percent) 3/	7.5	6.1	6.0	11.3
External sector				
Current account balance	-1.4	-4.4	-6.9	-9.4
Overall balance	0.3	-0.1	-0.2	1.2
External nonfinancial public sector debt	9.8	8.8	7.8	8.5
Debt service ratio 4/	5.2	5.0	4.2	5.5
Real effective exchange rate (depreciation -)	-3.9	-3.4	0.5	2.8
Gross international reserves (in millions of U.S. dollars)	173.6	170.6	163.0	218.0

Sources: The Central Bank of The Bahamas; Ministry of Finance; and IMF staff estimates.

1/ Estimated on the basis of partial indicators.
2/ Calculated as the number of stopover visitors times the estimated average length of stay.
3/ In relation to liabilities of the financial system to the private sector at the beginning of the year.
4/ Public sector debt service in percent of receipts from merchandise exports and tourism.

Press Information Notice (PIN) No. 98/10
FOR IMMEDIATE RELEASE
February 25, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Barbados

The IMF Executive Board on January 30, 1998 concluded the 1997 Article IV consultation[1] with Barbados.

Background

Barbados' economic performance has improved considerably in recent years due to good economic management and a more favorable external environment. Subsequent to a recession in 1990–92 and a slow recovery in 1993, **real GDP** growth averaged 3.5 percent a year during 1994–95. Growth accelerated to 5 percent in 1996, based on a recovery in sugar output from a drought in 1995 and a strong expansion in tourism, commerce, and construction. The performance of these sectors remained relatively strong in 1997, when real GDP is estimated by the Central Bank of Barbados (CBB) to have increased by 4.3 percent.

Inflation was low during 1994–96 (an average of 1.7 percent). However, prices rose by 7 percent in January 1997 with the introduction of a value-added tax (VAT); the largest increase was recorded in the prices of domestically produced food products, which previously were not subject to consumption taxes. Subsequent to the zero-rating of a basket of food items, prices declined in October 1997, and for 1997 as a whole prices increased by 3.6 percent. Barbados' real effective exchange rate, as measured by relative consumer prices, depreciated by 5 percent during 1994–96, but is estimated to have appreciated by 5 percent in 1997 reflecting in part the

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

appreciation of the U.S. dollar, to which the Barbados dollar is pegged.

There has been considerable wage restraint in recent years and stable industrial relations, facilitated by two successive prices and incomes protocols among the government, employers, and labor unions. The **unemployment rate** has declined substantially; it fell from 25 percent at the end of 1992 to 12.2 percent at the end of 1997; real wages are estimated to have declined by 7.5 percent in 1992 and to have remained about constant during 1993–96.

Reflecting a considerable strengthening of public sector saving and a decline in public investment (both relative to the late 1980s and 1990), the underlying **fiscal position** (excluding nonrecurrent operations) was in surplus during FYs 1991/92–1995/96 (April–March); during this period, small deficits in the central government were more than offset by the surpluses of the National Insurance Scheme. In FY 1996/97, however, the fiscal position shifted from a surplus of 2 percent of GDP in FY 1995/96 into a deficit of 0.8 percent of GDP as a substantial increase in central government investment was accompanied by a decline in central government saving. The underlying fiscal position is projected to revert to a small surplus (0.8 percent of GDP) in FY 1997/98.

The introduction of the **VAT** in January 1997 represented the culmination of the process of tax reform initiated in 1992 to streamline and improve the efficiency of the tax system. The VAT is broad based and has a rate of 15 percent, except for hotel accommodations that have a rate of 7.5 percent. To alleviate the impact of higher food prices on the poor, in early 1997 the government increased the minimum pension and cash grants to welfare recipients, and, more recently, zero-rated a number of basic food items effective October 1997. The government has proposed a regime of price controls on a number of zero-rated food items but these have not been implemented so far.

The main objective of **monetary policy** is to preserve the long standing exchange parity with the U.S. dollar. The net domestic assets of the CBB have declined steadily in recent years, as the public sector shifted from net debtor to the CBB to net creditor. The overall credit expansion by the banking system has been restrained.

During the 12 months ended June 1997, commercial banks were very liquid due to a rapid growth of broad money (associated with a strong balance of payments performance) and sluggish private demand for credit. During July–September 1997, the CBB conducted open market sales of treasury bills and withdrew government deposits from commercial banks. This policy, together with a recovery in credit to the private sector, led to a significant reduction in commercial banks' excess reserves. Also, the treasury bill rate which had declined steadily since June 1996 to 2.6 percent in June 1997, began to increase reaching 4.8 percent in December 1997. Bank lending rates remained virtually unchanged during this period notwithstanding the fact that the CBB lowered the minimum deposit rate from 5 percent to 4 percent in May 1997.

The **external current account** is estimated to have been in surplus in recent years. The surplus is estimated to have declined in 1997; imports grew rapidly as businesses rebuilt the inventories that were depleted prior to the introduction of the VAT. By December 1997 net international

reserves of the monetary authorities were US$271 million or 130 percent of base money compared with US$170 million or 100 percent of base money at end-1995.

In the last few years there have been structural reforms in the financial system (the closure and restructuring of two state banks), and in the tax and trade areas, and divestment of two partially state-owned enterprises. More recently, new financial legislation became effective in July 1997, strengthening prudential supervision along the lines of the Basle Accord, improving standards on capital adequacy, loan loss provisioning, liquid assets ratios, and limiting concentration of ownership and credit to related parties. In agreement with other members of the Caribbean Common Market, import duties were lowered in April 1997 to a range of 5–25 percent from 5–30 percent, and the special import surcharges that replaced several nontariff barriers in early 1994 are being phased out, albeit a slower pace than initially envisaged.

Executive Board Assessment

Executive Directors commended the authorities for the maintenance of restrained fiscal and incomes policies, which had contributed in recent years to price stability, economic growth, a sharp reduction in unemployment, and the strengthening of the external position. They welcomed the progress made by the authorities in improving the efficiency of the tax system through the successful introduction of the VAT. They also welcomed the adoption of new financial legislation that reinforced the regulatory and supervisory power of the central bank over commercial banks.

Directors nonetheless noted a number of economic concerns. In particular, the main export sectors continued to face relatively high costs and intense competition, and unemployment remains high. The fiscal position, although relatively strong, has weakened in the past two years, and the level of the public debt remains relatively high for a small economy that is vulnerable to adverse exogenous shocks. Directors, therefore, stressed the need to consolidate the recent gains and lay the basis for sustained low-inflation growth by continuing to pursue appropriate policies, including, in particular, fiscal consolidation and structural reforms aimed at enhancing the economy's flexibility and competitiveness.

Directors also stressed the need for continued fiscal and wage restraint to help preserve the exchange rate peg, which is a key element of the authorities' economic strategy. They noted that, while the current exchange rate seemed compatible with the maintenance of reasonable levels of economic activity and a strong external position, it would be crucial to enhance external competitiveness by promoting labor market flexibility and moving more rapidly with structural reforms in certain areas.

Pointing to the likely widening of the central government fiscal deficit in the next year, Directors emphasized that public sector savings should be increased to accommodate the required levels of development spending. They cautioned that the current fiscal stance would not permit a reduction in the public debt relative to GDP, and might not lead to a sufficiently strong external position over the medium term. Therefore, they recommended that the authorities aim at achieving a sound fiscal position over the medium term by limiting the central government deficit and by strengthening the finances of the public enterprises.

Directors suggested that, to achieve this fiscal consolidation objective, while maintaining adequate levels of public investment, the authorities should reduce central government current expenditure relative to GDP, including by limiting fiscal support to public and quasi-public enterprises. In this regard, they acknowledged the progress made in the reform of certain public enterprises, but stressed the need to take measures to improve their financial position, including through the setting of appropriate public service rates. They also saw a need to reduce costs in the quasi-public sugar industry and to limit the government's financial involvement in the tourism sector.

In the monetary area, Directors recommended greater use of indirect monetary instruments, the elimination of the interest rate floor on deposits, and the gradual liberalization of the capital account supported by the further strengthening of financial supervision. In this regard, Directors advised the authorities to improve the regulatory framework and supervision of financial institutions that are not supervised by the central bank, as well as to take steps to strengthen the competitiveness of the financial system. In light of the strong growth of private sector credit and the decline in international reserves that took place during the second half of 1997, Directors cautioned that credit conditions should be monitored closely, and they advised the authorities to be prepared to tighten monetary policy if excess demand pressures begin to develop.

Directors remarked that wage restraint and stable labor relations had made an important contribution to economic growth and employment in recent years. They recommended renewal of the income protocol to facilitate the maintenance of stable labor relations and wage restraint. They stressed the need for more flexible work rules and practices, and also encouraged the authorities to review the severance payments regime, with a view to reducing labor costs and enhancing labor flexibility, and integrating it better with the social safety net. Such improvements, together with the authorities' plan to strengthen education and training, should help increase the adaptability of the labor force and address the unemployment problem.

Directors noted that data weaknesses hampered the economic analysis, and urged the authorities to improve the availability and provision of data for surveillance.

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Barbados: Selected Economic Indicators

	1993	1994	1995	1996	Prel. 1997
	(Annual percentage changes; unless otherwise specified)				
Output and prices					
Real GDP	0.8	4.0	2.9	5.2	4.3
Tourist arrivals	2.7	7.5	3.9	1.1	5.6
Consumer prices (12-month increase) 1/	-1.0	0.5	2.8	1.8	3.6
Unemployment rate (in percent of the labor force) 2/	22.1	21.2	16.4	14.3	12.2
Real effective exchange rate (depreciation -) 3/	0.5	-3.5	-1.3	-0.8	5.0
Money and credit					
Net domestic assets 4/	3.8	1.5	3.1	4.7	5.2
Money and quasi-money	5.1	7.8	4.8	10.5	8.0
	(In percent of GDP at market prices)				
Public sector 5/6/					
Public sector underlying balance (deficit-)	0.6	2.3	2.1	-0.8	0.8
Central government overall balance	-1.6	-0.8	-0.3	-2.9	-1.0
National Insurance Scheme	2.2	2.1	2.3	2.4	2.4
Public enterprises	0.0	1.0	0.1	-0.3	-0.6
Total public debt 7/	79.0	76.7	69.6	66.7	64.3
External public debt 7/	27.1	25.5	22.3	20.6	19.6
Savings and investment					
Gross domestic investment	12.7	13.4	14.1	12.7	15.7
Gross national saving	17.0	21.1	19.0	16.5	18.4
External sector					
External current account	4.3	7.7	4.9	3.8	2.7
Overall balance of payments (in millions of U.S. dollars)	21.1	59.2	40.9	87.2	14.5
Net official international reserves					
(Percentage of base money)	45.2	85.5	97.7	112.3	130.5
(Months of retained imports)	1.6	2.7	2.9	4.0	3.8

Sources: Barbadian authorities; and IMF staff estimates and projections.

1/ The increase in 1997 reflects the impact of the introduction of a value-added tax in January 1997.

2/ End of period.

3/ As measured by relative consumer prices. The appreciation in 1997 reflects the domestic price rise related to the introduction of the value-added tax in January 1997 and the appreciation of the U.S. dollar.

4/ In relation to liabilities of the banking system to the private sector at the beginning of the period.

5/ Fiscal year (April-March).

6/ Excludes nonrecurrent operations.

7/ Includes debt of the central bank, including debt to the IMF.

Press Information Notice (PIN) No. 98/11
FOR IMMEDIATE RELEASE
March 3, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Belgium

The IMF Executive Board on February 23, 1998 concluded the 1997 Article IV consultation[1] with Belgium.

Background

Growth in 1997 was more rapid than anticipated, as strong external demand was complemented by an acceleration of domestic spending. Private consumption picked up pace, while corporate investment continued to expand. The recovery of household and business confidence has owed much to firm macroeconomic policies, particularly the decisive reduction of the fiscal deficit. Employment growth, however, remains weak. Recent economic performance thus reflects success in reducing macroeconomic imbalances, but also persisting structural problems.

Economic activity accelerated markedly in 1997, with GDP rising by 2.7 percent. While the recovery was export-led, domestic demand growth was stronger than projected. Corporate investment continued to expand, reflecting capacity pressures, lower interest rates, higher profits and strong foreign demand. Private consumption proved more robust than projected earlier, growing by 2.1 percent: its acceleration over the past four years, despite little growth in real disposable income, reflects a decline in precautionary saving as household confidence has recovered. Wages are tracking below the norm for 1997-98 (a ceiling of some 3 percent at an annual rate), and inflation has been well below 2 percent. The unemployment rate edged down slightly to some 12½ percent (9½ percent on an OECD standardized basis), with some three-quarters of the total estimated to be structural—concentrated among youths and the long-term

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

jobless, and with striking local variations in unemployment. Some shortages of high-skill labor are reported; but job creation remains weak, and mobility low. The current account surplus rose to some 5 percent of GDP over the past decade, with gains in the terms of trade and in investment income. The direct investment account, meanwhile, was in surplus, partly as a result of inflows for fiscally-privileged corporate headquarter activities, and foreign participations in the service sector; offsetting movements included outward portfolio investment and public debt repayment.

Monetary policy has continued to be firmly geared to the deutsche mark link. Long-term interest rates are now essentially at par with rates in Germany, and the short-term differential is small. With a real effective exchange rate depreciation of some 7 percent over the past two years, and a decline in interest rates, monetary conditions have eased notably. Market interest rates rose in October (when official rates mirrored developments in Germany), but have recently eased again. Since 1992, ***fiscal policy*** has been directed firmly to deficit reduction, despite an adverse cyclical setting, and the structural deficit has been cut by over 6 points of GDP. The debt ratio has fallen by 13 points from a 1993 peak. However, this reflected mainly lower interest costs and, until recently, higher taxes. The 1997 deficit goal was 2.9 percent of GDP. Modest spending cuts were largely durable, but little decline in the primary spending ratio was targeted; and civil service pension reform powers expired unused. Implementation was tight; and with strong revenues and lower-than-projected interest rates, it proved possible to cut the deficit to 2.1 percent of GDP—well below target. The 1998 budget aimed for an overall deficit of 2.3 percent of GDP, but this was recently cut to 1.8 percent of GDP. Revenue measures include an easing of social contributions, with minor tax offsets. Primary spending is to rise by close to 2 percent in real terms.

Labor market policies have tended to focus on the demand side, with pay norms in force for much of the past 15 years, and targeted cuts in social contributions—although the tax burden on labor income remains heavy. On the supply side, problems remain: unemployment benefits taper down over time, but without a final cut-off, and are not subject to strong job-search/training tests. Effective marginal tax rates on households are very high in some cases when the unemployed find work. Restraints remain on agency hiring and fixed-term work. Wage norms have safeguarded competitiveness but compressed differentials. Labor contracts are legally binding on all firms in a sector; and public support for early retirement has in the past been widespread. In the ***product markets***, with EU policies, change is underway; but reforms have yet to reach full fruition; slow job creation reflects in part remaining restrictions in services such as distribution.

The ***short-term outlook*** is for growth to continue at above potential, but with some slowing as a result of weaker expansion in foreign markets. Although exports to Asia are very modest, the main risk to the outlook lies in the impact of developments there on the global environment, including Belgium's competitiveness in third markets. On the positive side, market interest rates have declined in recent months. GDP is projected by the staff to grow by 2.6 percent in 1998. Although skill shortages may widen in the labor market, little pressure on prices is expected.

Executive Board Assessment

Executive Directors commended the strong macroeconomic and—especially—fiscal policies pursued by the authorities in recent years, which had yielded a number of impressive achievements and brought Belgium to the threshold of EMU. These policies

had helped to lower risk premiums, trigger a recovery of investment, and strengthen household confidence. As a result, growth was becoming more balanced, with strong export growth complemented by rising domestic demand. At the same time, however, Directors remained concerned about the continuing serious structural problems in the economy, in particular the high level of unemployment and the high, albeit declining, ratio of public debt to GDP. Directors therefore urged the authorities to take advantage of the current economic recovery to address decisively underlying structural issues, in particular those relating to the functioning of the labor and product markets, and the outlook for the public finances—including the heavy tax burden on labor income. In this regard, Directors underlined the crucial interlinkages recognized by the authorities, between labor market reforms and fiscal adjustment, and noted therefore that the medium-term sustainability of the fiscal position would be much improved by such reforms.

Directors noted that monetary policy, based on the deutsche mark link, had achieved high credibility. This had contributed to the decline in inflation and interest rates in recent years, and had helped to lay the basis for the present economic recovery. Directors saw the prospective monetary union as offering opportunities to strengthen economic performance. However, they stressed that this would depend on action to improve the flexibility of the economy, by creating sufficient room for fiscal stabilizers to operate, and by imparting greater responsiveness to labor and product markets.

Directors praised the firm implementation of fiscal policy in 1997, which had cut the deficit to a level well below target, against the background of favorable economic trends. They noted, however, that this performance reflected mainly interest rate reductions and revenue increases rather than reductions in primary spending. For 1998, Directors welcomed the announcement that the deficit objective had been revised from 2.3 percent of GDP to 1.8 percent of GDP.

Directors considered that fiscal consolidation remained a very high priority for 1998 and beyond, and should be designed to ensure a convincing safety margin under the Stability and Growth Pact, as well as a decisive cut in the debt burden before the emergence of demographic pressures. Directors considered that, over the medium term, fiscal policy should also aim to secure a durable cut in the tax burden. To achieve these twin goals, it would be crucial to secure a slowdown in primary spending to well below the trend growth of GDP. This would require further structural reforms in health care and pensions, as well as greater prioritization of spending; moreover, several Directors stressed that it was particularly important for the regions and communities to restrain spending firmly. For 1999, Directors called for a strong fiscal effort, with a view to achieving structural balance over the medium term. In addition, there was need to reach agreement on medium-term spending ceilings for each level of government, to create scope for a significant cut in the tax burden on labor income, which should reduce total labor costs. In this regard,

Directors supported the authorities' intention to reduce social security contributions by employers, in a fiscally neutral manner, and urged that this be achieved as far as possible by offsetting expenditure cuts.

There was a clear consensus that improving the prospects for employment creation was a crucial priority for the period ahead, and one which could make a major long-run contribution to strengthening economic performance and the sustainability of the public finances. Directors noted that the unemployment problem was a complex issue, displaying large disparities among regions and skill levels and reflecting a number of difficult problems in the labor market related in particular to the benefit and tax structure, and limited wage differentiation among sectors and firms. They therefore called for measures to liberalize labor market conditions. A key priority in this regard was to improve the opportunities and incentives for the young to enter employment and training. To that end, unemployment benefits should be made more dependent on genuine efforts to seek work or training, which would require better coordination among the welfare, employment, and training services. Recent steps to address tax traps and pare back early retirement were welcomed, but further progress in these directions was viewed as crucial. Several Directors expressed their doubts regarding suggestions to shorten working hours, and stated in particular that, in any event, any such reduction should not result in an increase in labor costs.

Directors noted that the performance of the economy, including in job creation, would also benefit from a strengthening of competition in product markets. European Union policies and market pressures would be major forces for change, leading to further rationalization in such sectors as telecommunications, power, transport, and banking. In this connection, Directors stressed the need to deregulate market services, such as distribution, so that efficiency gains in mature industries were coupled with vigorous job creation elsewhere.

With a strengthening of structural policies, Directors considered that the Belgian economy stood to gain strongly from wider economic integration in Europe, including an enlargement of the European Union—objectives supported by the authorities.

With regard to development assistance, Directors expressed concern about the recent impact of budgetary restraint, while hoping that greater selectivity might mitigate the economic impact of this; they encouraged the authorities to accord higher priority to protecting aid flows, with a view to reversing the downward trend.

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Belgium: Selected Economic Indicators

	1994	1995	1996	1997	1998 1/
Real economy (change in percent)					
Real GDP	2.4	2.1	1.5	2.7	2.6
Domestic demand	1.4	1.7	1.4	2.3	2.2
CPI (year average)	2.4	1.5	2.1	1.6	1.5
Unemployment rate (in percent)	12.9	12.9	12.7	12.5	12.3
Gross national saving (percent of GDP)	21.9	22.8	22.5	23.0	23.2
Gross national investment (percent of GDP)	17.6	17.9	17.5	17.7	17.8
Public finance (percent of GDP)					
Federal government balance (deficit -)	-4.8	-4.0	-3.0	-2.3	-1.9
General government balance (deficit -)	-4.9	-3.9	-3.2	-2.1	-1.8
Public debt	133.5	131.2	126.9	122.2	118.5
Money and interest rates					
M2 (end of year, percent change) 2/	2.8	4.9	6.4	3.6	...
Money market rate (in percent)	5.7	4.8	3.2	3.5	...
Government bond yield (in percent)	7.8	7.5	6.5	5.8	...
Balance of payments of BLEU (in percent of GDP)					
Trade balance (percent of GDP)	2.9	3.5	3.2	3.4	3.8
Current account (percent of GDP)	5.4	5.3	5.2	5.6	6.0
Official reserves (US$ billion) 3/	13.9	16.2	17.0	16.2	...
Exchange rates					
Exchange rate regime			Member of ERM		
Present rate (February 23, 1998)			BF 37.47 per US$1		
Nominal effective exchange rate (1990 =100)	105.1	109.3	107	102.7	...
Real effective exchange rate (1990 = 100)	105.6	110.7	108	103.5	...

Sources: Data provided by the authorities; and IMF staff estimates.

1/ Staff projections.
2/ For 1997, August.
3/ Excluding gold; for 1997, December.

Press Information Notice (PIN) No. 98/28
FOR IMMEDIATE RELEASE
April 10, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Botswana

The IMF Executive Board on March 13, 1998 concluded the Article IV consultation[1] with Botswana.

Background

Botswana's sound macroeconomic policies and the harnessing of its substantial mineral resources, together with a stable democratic system, have helped transform Botswana from one of the world's poorest countries in the 1960s and 1970s to a middle-income country in the 1990s. Real GDP growth, which averaged 16 percent in the 1970s and 11 percent in the 1980s, was underpinned importantly by the exploitation of Botswana's abundant diamond resources; the diamond sector accounts for about 30 percent of GDP, and about two-thirds of exports and central government revenue. In the early 1990s, economic growth slowed markedly reflecting a weakening in the international diamond market and several years of serious drought. However, real GDP growth rebounded due to expanded capacity in the diamond sector to an annual average of almost 7 percent in 1995-97. Despite strong real GDP growth, employment growth in the formal sector has remained sluggish, at slightly over 1 percent a year, and unemployment is estimated at around 20 percent of the labor force. Consumer price inflation has declined over recent years, reaching 7.8 percent for the year ended December 1997; it has moved roughly in line with the South African inflation rate during 1997.

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

Botswana's strong economic performance has been buttressed by sustained fiscal surpluses over many years. In 1996/97, the government's overall fiscal surplus was equivalent to 7.6 percent of GDP, reflecting marked gains in mineral tax revenue and increased interest income on sharply higher foreign exchange reserves, as well as restraint in government spending. A fiscal surplus equivalent to 6.6 percent of GDP was recorded in 1997/98. The 1998/99 budget, announced on February 9, 1998, projects a surplus equivalent to almost 1 percent of GDP for the fiscal year, which reflects lower mineral tax revenue owing to a projected slowdown in diamond sales, particularly to Asian markets, and growth in government spending, due in part to an acceleration in the implementation of projects.

In recent years, broad money has expanded rapidly, due principally to a substantial increase in the net foreign assets of the banking system. Bank credit to the private sector has revived in recent months, owing largely to increased lending to the household sector. The authorities continued their efforts to absorb excess liquidity in the banking system through open market operations. Despite this excess liquidity, interest rates on financial assets have remained positive in real terms, comparable to those in major international financial centers.

The strength of Botswana's external position, as reflected in its sizable current account surplus which improved to an estimated 13 percent of GDP in 1996, has contributed to the accumulation of substantial official reserves, amounting to US$5.2 billion by end-1996, equivalent to about 35 months of imports of goods and services. By end-1997, international reserves had risen further to US$5.7 billion. Over the years, Botswana's exchange rate policy has accorded a high priority to preserving competitiveness to help promote economic diversification and expand employment in the nontraditional industries, while giving due attention to containing the inflationary impact of exchange rate developments. The nominal and real effective exchange rates at end-November 1997 had depreciated by 7 percent and 3 percent, respectively, compared with two years earlier. Botswana has fully liberalized external current account transactions (in November 1995, Botswana accepted the obligations of the IMF's Article VIII), and has also liberalized most capital account transactions.

The Eighth National Development Plan (NDP8) covering the 1997/98-2002/03 period has economic diversification as its central theme, which is considered critical for generating employment, alleviating poverty, and reducing income inequality. Botswana's strong external position provides considerable flexibility to pursue these objectives in an increasingly liberalized external trade and payments environment. The strategy incorporates further external sector liberalization, rationalization of government activities aimed particularly at promoting employment through selective public works programs, and further development of the infrastructure where present inadequacies are hindering economic growth. In preparation for exposure to greater competition, the public enterprise

sector will be restructured through rationalizing and downsizing, privatization, and productivity improvements. With unemployment affecting primarily the young and unskilled, the quality of education is to be improved, in cooperation with the private sector, at all levels, including through the development of technical, entrepreneurial, and managerial skills.

Improvements have occurred in the preparation and availability of Botswana's economic statistics. The authorities are continuing with their efforts to secure needed further improvements in preparing the national accounts, fiscal, monetary, and balance of payments data.

Executive Board Assessment

Executive Directors commended the authorities for their continued prudent approach to economic policy, which had contributed to sustained economic growth, low inflation, and a strong external position. Noting that Botswana's large dependence on the diamond sector remained a source of vulnerability, Directors underscored the need for the authorities to pursue additional structural policies aimed at economic diversification over the medium term, while maintaining prudent macroeconomic policies. Such policies would be essential to boost employment opportunities and to reduce income inequality.

Noting the prospect for a substantial reduction in the fiscal surplus budgeted for 1998/99, Directors encouraged the authorities to take actions to tighten the fiscal stance so as to preserve macroeconomic stability. In this regard, they stressed that the recent and projected growth in government expenditure, while helpful in easing some key structural bottlenecks in the economy, ran the danger of providing an excessive fiscal stimulus. Directors were of the view that undue front-loading of the development projects envisaged in the plan should be avoided, in light of the limited absorptive capacity of the economy; and lower priority expenditure should be scrutinized rigorously to allow increased budgetary allocation for well-targeted social safety nets and essential social sectors. Attention should also be paid to reducing, over time, the government's fiscal dependence on the diamond sector and on taxes related to external trade, by broadening the base of the sales tax and replacing it eventually with a value-added tax.

Directors underscored the need to pursue the restructuring and privatization effort in the public sector more vigorously, particularly in areas that would reduce reliance on budgetary resources.

Directors considered that monetary policy had been appropriately focused on maintaining positive real interest rates on financial assets. However, financial markets needed to be deepened and the array of financial assets widened, especially in view of the heavy dependence on Bank of Botswana certificates to absorb excess liquidity. A secondary market for these certificates and long-term debt instruments could be developed. Furthermore, adoption of a comprehensive program of financial and technical support enabling small- and medium-scale enterprises to borrow from the commercial banks could increase financial intermediation.

Directors welcomed the recently announced further steps in exchange control liberalization, and encouraged the authorities to continue their efforts in this area. Directors considered that the

policy of pegging the Botswana pula to a basket of currencies had served Botswana well, and encouraged the authorities to make the composition of the basket transparent.

Press Information Notices (PINs) are issued, at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

Botswana: Selected Economic Indicators

	1994	1995	1996	1997	1998 1/
			(Percentage change)		
Domestic economy					
Real GDP	3.1	7.0	6.8	4.2	3.5
Consumer prices (period average)	10.6	10.5	10.1	8.8	7.6
			(In millions of U.S. dollars)		
External economy					
Exports, f.o.b.	1,725.1	1,875.4	2,160.7	2,232.8	3,035.2
Imports, f.o.b.	-1,457.9	-1,350.7	-1,579.1	-1,436.1	-1,939.2
Current account balance	504.2	239.2	337.9	662.7	819.5
(In percent of GDP)	12.1	5.4	6.9	13.1	16.0
Gross official reserves (end of period)	4,401.5	4,695.5	5,243.9	5,675.0	6,200.0
(In months of imports)	31.6	27.8	35.3	28.9	29.3
Debt service 2/	4.5	3.4	3.3	2.5	3.1
Change in real effective exchange rate (in percent) 3/	-1.0	-3.5	-9.9	0.5	...
			(In percent of GDP)		
Financial variables					
Central government overall balance 4/	1.6	1.9	7.6	6.6	0.9
Central government primary balance 4/	2.3	2.6	8.1	7.1	1.4
Change in broad money (M2) (in percent) 5/	7.0	-3.3	16.5	25.1	...
Bank of Botswana lending rate (in percent per annum)	13.5	13.0	13.0	12.5	...

Sources: Botswana authorities; and IMF staff estimates and projections.

1/ Staff projections.

2/ In percent of exports of goods and services.

3/ (-) = depreciation.

4/ Year beginning April 1.

5/ For 1997, September.

Press Information Notice (PIN) No. 98/18
FOR IMMEDIATE RELEASE
March 13, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Brazil

The IMF Executive Board on February 11, 1998 concluded the 1997 Article IV consultation[1] with Brazil.

Background

In 1997 Brazil continued to reduce its **inflation rate** to under 5 percent, reflecting a moderation in labor costs and import prices, as well as a good harvest. **Real GDP** grew by an estimated 3.0 percent, compared with 2.9 percent in 1996. Growth was led by domestic demand, especially investment. The trade deficit widened, albeit at a declining rate as the year progressed, reflecting a sharp increase in imports. Manufactured exports recovered significantly, however, in the second half of the year. The rise in the trade deficit, together with a deterioration in net service payments, contributed to an increase of the **external current account** deficit to US$33.4 billion in 1997 (4.2 percent of GDP) from US$24 billion in 1996 (3.2 percent of GDP). More than half of the current account deficit was financed by **foreign direct investment**, which increased strongly in 1997, partly as a result of the privatization program. In 1997 as a whole, **international reserves** declined by about US$8 billion (all of which occurred during the financial market turmoil in late October) to a level of about US$52 billion, equivalent to 8.2 months of imports of goods and nonfactor services. Reserves have subsequently recovered to about US$58 billion by end-February 1998.

Preliminary financing data indicate that the overall **fiscal position**, as measured by the public sector borrowing requirement, which remained at 5.9 percent of GDP, was essentially unchanged in 1997. The primary deficit, however, increased from 0.1 percent of GDP in 1996 to

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

0.7 percent of GDP in 1997. This result reflects mainly the outturn for the social security and increased spending by the states (partly to eliminate arrears or contingent liabilities) financed by large privatization receipts. **Monetary policy** remained cautious. In April 1997, the central bank departed from the policy of gradually reducing interest rates in line with the decline in inflation, leaving its basic intervention rate unchanged at 20.7 percent until the end of October. The authorities allowed the *real* to depreciate within the exchange rate band by about 0.6 percent a month against the U.S. dollar, more than the inflation differential between the two countries.

In late October 1997, Brazil's currency came under pressure following the turmoil in financial markets in Asia. The authorities reacted swiftly by doubling the central bank intervention interest rate on October 30, 1997 to 43 percent, and on November 10, 1997 announced the adoption of a comprehensive fiscal package equivalent to about 2½ percent of GDP. These actions were instrumental in improving market expectations, and promoting a reflow of capital and the substantial recovery of international reserves to date in 1998. The reestablishment of calm in financial markets has allowed a sizable reduction (over 15 percentage points at an annual rate) of interest rates in the last couple of months.

Executive Board Assessment

Directors commended the authorities for their quick and decisive policy response to the strong pressures on the real in late October, noting that those actions—the doubling of interest rates and the quick passage of a strong fiscal package—had played an important role in limiting the contagion effects from the Asian turmoil in Brazil and the rest of Latin America. Directors stressed that the steady implementation of the fiscal adjustment measures, the early passage of the pending structural fiscal reforms, and prudent monetary policy would be essential to ensure a sustained reduction of the current account deficit, minimize Brazil's vulnerability to the continuing volatility in international financial markets, and realize its full economic potential.

Directors noted that Brazil's economy had continued to perform well in 1997, with per capita real GDP showing significant growth for the fifth consecutive year, and consumer price inflation falling to under 5 percent. They also noted the progress made in strengthening the financial system and in accelerating the privatization program. However, they noted that the external accounts had continued to deteriorate, albeit at a decelerating pace as the year had progressed.

While Directors were encouraged by the recovery of manufactured exports, strong growth of direct investment in 1997, and by the prospect of a further decline in the current account deficit in 1998, they noted that those projected improvements in the external accounts were predicated on a stable international environment and sustained export growth and, therefore, developments would need to be carefully monitored. In view of Brazil's high level of external debt and debt service in relation to exports, Directors stressed the importance of securing further reductions of the current account deficit in subsequent years, through a sustained improvement in competitiveness and further growth and diversification of exports.

Directors generally supported the authorities' policy of seeking a gradual depreciation of the real exchange rate within the current band system, taking into account productivity developments.

Most Directors felt that, in the present unsettled market conditions, any significant modification of exchange rate policies could be misinterpreted and could lead to a loss of confidence.

Noting the recent reduction of maturities of new public debt and the increase in the share of domestic public debt with a foreign exchange guarantee, Directors urged the authorities to step up their efforts to revert soon to the earlier trends toward lengthening the average maturities of debt and reducing the share of foreign exchange indexed debt.

Directors noted that the implementation of the authorities' fiscal policy package as envisaged, together with the use of most of the privatization receipts for debt reduction, would facilitate a decline in the overall public sector deficit and debt and, therefore, a further sustained reduction in interest rates during the course of the year. Directors stressed the importance of fiscal consolidation as a means of continuing to raise domestic savings. They also emphasized the importance of resisting spending pressures that might arise during a year of general elections, and welcomed the authorities' readiness to adopt additional measures if needed.

Directors commended the progress made in setting the finances of the states on a more sustainable path, in particular through the restructuring of their debt at substantially reduced interest rates. To ensure long-term sustainability, it was essential that debt restructuring be accompanied by the negotiation and firm implementation of strong fiscal adjustment programs by the states, and by the use of a large share of their privatization proceeds to reduce debt. Directors stressed the importance of speedily concluding the negotiations of such programs, and emphasized that expenditure restraint will be key to the states' fiscal adjustment in 1998. Moreover, the federal government will need to monitor closely and enforce firmly the implementation of those programs, and ensure that the states fully service their rescheduled debt.

Directors welcomed the authorities' success in privatizing public enterprises, both at the federal and state levels. They noted that the privatization process would allow for much needed investments by the private sector, which, along with efficiency gains, would establish a better foundation for future economic growth.

Directors welcomed the authorities' recent progress in obtaining Congressional approval of the proposed constitutional reforms concerning the social security and public administration system, and the prospect of final approval of that legislation in the near future. Some Directors noted, however, that it would be desirable to move forward as soon as possible with a further, more comprehensive reform of the social security system. Directors welcomed the steps taken in the context of the fiscal package to eliminate some important regional fiscal incentives and to streamline direct taxation, as well as the authorities' intention to put forward soon proposals for a comprehensive fiscal reform and their efforts to improve efficiency in health and education spending. Directors believed that the efforts being undertaken to increase flexibility in the labor market were a key element of the modernization strategy. They also took note of the recent improvements in key social indicators, and encouraged the authorities to continue to strive for a reduction of poverty and income inequality.

Directors supported the authorities' intention further to reduce interest rates at a pace that will prove consistent with the maintenance of stable conditions in financial and foreign exchange

markets. They also noted that, as a result of the substantial progress made in the past couple of years in strengthening their balance sheets, the banks were in a better position than in 1995 to withstand the adverse effects of high real interest rates and a slowdown of economic activity on the quality of their portfolios. Nevertheless, Directors cautioned that the authorities would need to continue their close monitoring of the large banks and their ongoing program of thorough inspections of second-tier banks.

Directors also welcomed the authorities' ongoing efforts to strengthen bank supervision, with the support of the World Bank, and the measures taken recently to tighten capital adequacy standards, and urged the authorities further to strengthen efforts to improve their information on the consolidated foreign currency exposure of financial institutions and of enterprises.

Directors welcomed the significant progress that had been made in restructuring state banks, with two large banks privatized in 1997, and two other major banks scheduled for privatization in 1998. With respect to the other smaller state-owned banks with problems, Directors urged the authorities to continue their efforts to privatize or, if necessary, close them. As far as the federal banks were concerned, Directors noted that their capital appeared adequate at the present time, and stressed the importance of allowing them to conduct their operations on a strictly commercial basis. Directors also felt that, over the medium term, it would be desirable to further reduce the public sector's involvement in banking activities.

Directors encouraged the authorities to further liberalize trade, which would provide impetus to the modernization and development of the economy. Directors noted that import tariffs in Brazil remained high, and the dispersion of rates gave rise to high rates of effective protection in some sectors. Several Directors called for a reduction in the protection provided to the automobile sector. They also stated that the recently agreed increase in the common external tariff of Mercosur ran counter to the trade liberalization trend, and urged the authorities and their Mercosur partners to work toward an early reversal of this increase.

Directors urged the authorities to eliminate Brazil's remaining exchange restrictions and move quickly to accept the obligations under Article VIII, Sections 2, 3, and 4 of the Articles of Agreement.

Directors commended the authorities for their efforts to provide comprehensive economic data regularly and on a timely basis to the staff. They encouraged the authorities to take steps to further improve the comprehensiveness of financial sector and external debt statistics. With a view to improving the transparency of Brazil's economy to foreign financial markets, Directors agreed that it would be desirable that the authorities take the necessary steps to enable Brazil to subscribe to the Special Data Dissemination Standard.

Press Information Notices (PINs) are issued, at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

Brazil: Selected Economic Indicators

	1994	1995	1996	1997 1/
		(In percent)		
Domestic economy				
Change in real GDP	6.0	4.2	2.9	3.0
Unemployment rate	5.1	4.6	5.4	5.7
Change in consumer prices (end of period)	929.3	22.0	9.1	4.3
Change in consumer prices (year average)	2,149.0	67.3	16.5	6.0
		(In billions of U.S. dollars) 2/		
External economy				
Exports, f.o.b	44	47	48	53
Imports, f.o.b.	33	50	53	61
Current account balance	-2	-18	-25	-33
Direct investment	2	4	10	17
Portfolio investment	7	2	6	5
Capital account balance	15	32	34	26
Gross official reserves	39	52	60	52
Current account balance (in percent of GDP)	-0.3	-2.5	-3.2	-4.2
		(In percent of GDP) 2/		
Financial variables				
Public sector borrowing requirement	45.5	7.2	5.9	5.9
Change in broad money (in percent)	1,148.5	33.5	7.8	25.5
Monthly nominal interest rate (in percent)	25.2	3.6	2.0	1.9

Source: Brazilian authorities and staff estimates.

1/ Estimates.
2/ Unless otherwise noted.

Press Information Notice (PIN) No. 98/2
FOR IMMEDIATE RELEASE
January 21, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Cameroon

The IMF Executive Board on January 7, 1998 concluded the 1997 Article IV consultation[1] with Cameroon.

Background

After an eight-year period of economic decline, activity picked up in 1994/95 (July-June), reflecting the effects of the 1994 devaluation of the CFA franc. Real GDP, which had declined by an average of 4 percent during these years, rose by 3.3 percent in 1994/95 and by 5 percent in 1995/96. As the effects of the devaluation tapered off, inflation fell from 33.8 percent in 1993/94 (end of period) to 4.4 percent in 1995/96. Economic activity remained buoyant in 1996/97. Real GDP growth is estimated to have stabilized at 5 percent, a pace that appears to have continued in the early months of 1997/98. This growth was propelled by a substantial improvement in the tradable goods sectors. Inflation, which rose to 9.9 percent in the year to June 1997 (reflecting a temporary shortage of foodstuffs associated with unrest in neighboring countries), fell to 2.8 percent in November 1997. Mirroring the strong economic activity, total investment increased in relation to GDP by about 1 percentage point to 16½ percent; public and private savings both rose by 2 percentage points to about 15½ of GDP.

In the policy area, progress was made in strengthening government finances. However, budgetary improvements fell short of program targets under the 12-month Stand-by arrangement approved by the IMF Executive Board on September 27, 1995, particularly with regard to non-oil revenue, and noninterest expenditure, including wages, remained compressed. Also, the

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

implementation of structural reforms was slower than envisaged. In an effort to remedy these slippages, the Cameroonian authorities asked the Fund staff to monitor the execution of their adjustment program for 1996/97, so as to pave the way for an ESAF-supported program. While performance under the staff-monitored program in the first half of the fiscal year was mixed, the authorities took remedial actions to bring it back on track in the second half of the year, including in particular, the transfer to the budget of all the windfall revenue of the national oil company (SNH) accrued in the first half of the year. On this basis, the Executive Board approved Cameroon's request for a three-year arrangement under the ESAF.

Significant progress was made in strengthening the public finances. The primary budget surplus is estimated to have increased by about ½ of one percentage point to 5.8 percent of GDP in 1996/97, owing largely to higher-than-projected oil prices and the transfer of windfall oil revenue to the Treasury. However, non-oil revenue was below target, reflecting continued weaknesses in revenue-raising capacity. The improved overall budgetary outcome in 1996/97 enabled the authorities to make large external debt service payments and substantially reduce external payments arrears on nonreschedulable debt, totaling some US$450 million (5 percent of GDP).

Progress was made in 1996/97 in implementing structural reforms in the civil service, the public enterprise sector, the financial sector, and in reducing domestic payments arrears. Noteworthy are the completion of the long-eluded rehabilitation of the domestic banking system and the transparent privatization of the national rubber company.

Monetary developments in 1996/97 were characterized by a strengthening in money demand and an improvement in net foreign assets of the banking system, reflecting the gradual return of confidence in the banking system that followed its successful rehabilitation. Net foreign assets increased by CFAF 114 billion in the 12-month period ending June 1997, and total deposits in domestic banks rose by 7 percent during the same period, reversing a decline of 21 percent in the previous year; broad money increased by about 14 percent.

In the external sector, the 1994 devaluation of the French franc vis-à-vis the U.S. dollar helped to maintain the gains in competitiveness achieved since the devaluation of the CFA franc. As a result, total non-oil exports are estimated to have grown by almost 12 percent in volume terms in 1996/97, led by logs, coffee, cotton, natural rubber, and manufactured goods. In addition, oil exports are estimated to have increased by about 10 percent in volume; in value (SDR) terms oil exports increased by 36 percent benefitting in part from favorable international prices. In line with the strong growth of total demand, import volume increased by 19 percent. Reflecting the gains in the value of exports, the external current account deficit narrowed by about 1 percentage point of GDP, to 1.2 percent in 1996/97. Finally, there was an inflow of non-oil private capital into Cameroon, estimated at about 1 percent of GDP, marking a significant turnaround from developments in the early 1990s.

Executive Board Assessment

Executive Directors noted the continued buoyancy in economic activity—reflected in positive real per capita growth—the low inflation rate, and the progress made in strengthening public finances

and in implementing key structural reforms under the staff-monitored program for 1996/97. They also noted the efforts made to normalize relations with Cameroon's external creditors. Furthermore, Directors were encouraged by the good economic performance during the first quarter of 1997/98 under the program supported by the Enhanced Structural Adjustment Facility, but observed that this performance had to be seen only as a beginning of the adjustment process after a period of a poor track record and against the background of the recent favorable oil price developments. Against this background, Directors stressed the importance of strengthened policy implementation to demonstrate a firm and lasting commitment to macroeconomic stabilization and structural reform.

While noting some improvement in the conduct of fiscal policy, Directors emphasized the need to address the significant weaknesses remaining in both revenue-generating capacity and expenditure management. In this regard, they noted the worrisome backtracking on the forestry tax reform included in the program, and urged the authorities to reinstate as soon as possible these reform measures so as to reach the programmed revenue target. This measure, together with bold actions to improve tax administration and combat fraud, and to prepare adequately for the planned introduction of the value-added tax, would be crucial to broadening the tax base and achieving the revenue target.

On the expenditure side, Directors stressed the need to enhance efficiency, effectiveness, and accountability in government budgetary operations, and ensure adherence to spending priorities in favor of social services and infrastructure. They welcomed the authorities' request for Fund technical assistance on public expenditure management. They also noted that the unfreezing of civil service promotions and merit increases in February 1997 was a first step toward improving staff morale. Noting that civil service reform should be a priority, Directors called on the authorities to decompress the salary structure and rationalize civil service employment to keep the overall wage bill within a reasonable limit.

In the financial sector, Directors noted the completion of the long elusive rehabilitation of the banking system. Moreover, they encouraged the authorities to improve the functioning and soundness of the banking system through the removal of any remaining government involvement in all banking decisions following the rehabilitation and privatization of the banks; the active use of indirect monetary instruments; and the strengthening of bank supervision. Several Directors also encouraged the authorities to strengthen the independence of the regional banking commission and ensure that prudential regulations are observed.

Directors stressed the importance of accelerating structural reforms aimed at further reducing the public sector's share in the economy by pressing ahead with privatization and liberalization of the energy and transport sectors, so as to consolidate the gains in external competitiveness and allow Cameroon to achieve its growth potential. In this regard, they underlined the need to enhance transparency in the energy sector and to rehabilitate economic infrastructure.

Directors welcomed the rescheduling agreement reached with the Paris Club in October 1997. They called on the authorities to clear all remaining external payments arrears on nonreschedulable debt, as scheduled, and to remain current on all debt-service payments falling

due. Directors urged the authorities to make rapid progress toward concluding bilateral agreements with Paris Club creditors and to reach agreements on similar terms with non-Paris Club official and commercial creditors.

Directors stressed the need to improve further the quality and timeliness of the availability of Cameroon's core data.

Press Information Notices (PINs) are a new series of IMF press notices (see Press Release 97/21). PINs are issued, at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

Cameroon: Selected Economic Indicators, 1993/94-1997/98 1/

	1993/94	1994/95	1995/96	1996/97 2/	1997/98 Program
			In Percent		
Domestic economy					
Change in real GDP	-2.5	3.3	5.0	5.1	5.0
Change in consumer prices (end of period)	33.8	13.4	4.4	9.9 3/	2.0
			In millions of U.S. dollars 4/		
External economy					
Exports, f.o.b.	1,433	1,664	1,761	1,978	1,820
Imports, f.o.b.	1,017	1,074	1,201	1,347	1,376
Current account balance 5/	-327	-62	-219	-109	-200
Direct investment	105	101	120	126	122
Portfolio investment	111	125	146	158	119
Capital account balance	-266	-513	-433	-354	52
Current account balance (percent of GDP) 5/	-4.2	-0.8	-2.4	-1.2	-2.3
Of which: non-oil sector	-8.2	-4.3	-5.2	-5.7	-6.9
Change in real effective exchange rate (in percent) 6/	-24.7	-11.9	6.4	-2.6	...
			In percent of GDP 4/		
Financial variables					
Gross national savings	11.2	13.7	13.3	15.4	15.8
Gross domestic investments	15.3	14.5	15.7	16.6	18.0
Central government balance	-9.2	-3.2	-1.8	-1.0	-2.0
Primary balance	0.8	3.8	5.4	5.8	5.7
Change in broad money (in percent)	17.7	6.1	-5.1	13.8	13.0
Interest rate (in percent) 7/	12.5	8.8	8.0	7.5	...

1/ Fiscal year begins in July.
2/ Data provided by the Cameroonian authorities and IMF staff estimates.
3/ Inflation fell to 2.8 percent in November 1997.
4/ Unless otherwise indicated.
5/ Including grants.
6/ (+) = appreciation
7/ Discount rate (end of period).

Press Information Notice (PIN) No. 98/6
FOR IMMEDIATE RELEASE
February 19, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Canada

The IMF Executive Board on January 30, 1998 concluded the 1998 Article IV consultation[1] with Canada.

Background

Following a slowdown in 1995 and in early 1996, real GDP growth rose at an annual rate of 3¼ percent in the second half of 1996 and 4½ percent in the first three quarters of 1997. Activity has been supported by strong increases in private investment and personal consumption. With relatively weak growth in personal income, the strength in consumption can be attributed to declines in interest rates and increases in wealth associated with a sharp rise in stock prices. While excess capacity has declined in the past year, it is estimated that output was about 1¾ percent below potential in mid-1997. After edging up from 9½ percent in 1995 to near 10 percent in the latter part of 1996, the unemployment rate declined to 9 percent in July 1997 and remained at around that level through November 1997, before falling to 8.6 percent in December. For most of the period since 1993, core CPI inflation (the CPI excluding food, energy, and changes in indirect taxes) has been maintained within the lower half of the Bank of Canada's official target range of 1 to 3 percent. Core inflation was 0.8 percent (annual rate) at the end of 1997.

Since May 1995, the Bank of Canada has adopted a generally accommodative monetary policy. Beginning in the latter part of 1996, the Bank sought to maintain monetary conditions roughly unchanged, and in late June 1997, the Bank raised the operating band for the overnight interest

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

rate by 25 basis points to counter an easing in monetary conditions stemming from a depreciation of the Canadian dollar. The Bank moved to tighten monetary conditions modestly in October 1997, when it raised the overnight rate operating band by 25 basis points. At that time, it noted that there was growing evidence that the economy was expanding rapidly and absorbing unused capacity, and that indicators of future growth had been strong. In late November, in mid-December, and again in late January 1998, the Bank of Canada raised the overnight rate operating band by a total of 125 basis points to counteract an easing of monetary conditions, as downward pressure on the Canadian dollar increased sharply toward the end of 1997 and early in 1998, reflecting fallout from the financial crisis in Asia.

The current Government has reduced the federal fiscal deficit from 5.8 percent of GDP in 1993/94 (fiscal year ending March 1994) to 1.1 percent of GDP in 1996/97. Most of this improvement reflected the adoption of strict limits on spending, and the structural budget deficit (i.e., the estimate of the deficit measured at full employment) declined from 5 percent of GDP to around ½ percent of GDP over the period. The provinces also have moved to improve their budget positions in recent years, with the aggregate fiscal position of the provinces shifting from a deficit of 3.7 percent of GDP in 1992 (national accounts basis) to near balance in 1996. Nevertheless, the ratio of net general government debt to GDP increased from about 43 percent in 1990 to what now appears to be of peak of 67 percent in 1996; the ratio is expected to decline significantly in coming years.

After coming under bouts of pressure in the early 1990s, the Canadian dollar traded in a narrow range of 72–74 U.S. cents from mid-1995 to June 1997. In late June, its value slipped below 72 U.S. cents, but it rebounded after the Bank of Canada's move to raise short-term interest rates. Since mid-November, the Canadian dollar has been under downward pressure, reflecting market expectations that the financial crisis in Asia will have more of a detrimental effect on the Canadian than the U.S. economy, particularly through its impact on commodity prices. As a result, the Canadian dollar's value fell below 69 U.S. cents in January 1998. On a real effective basis, the Canadian dollar in December 1997 was about 2 ½ percent above its low in March 1995, but it was nearly 25 percent below its previous peak in June 1991. The external current account balance shifted from a deficit of $7½ billion (1 percent of GDP) in 1995 to a surplus of nearly $4 billion (0.4 percent of GDP) in 1996. In the first three quarters of 1997, the current account deteriorated substantially, registering a deficit of 1.8 percent of GDP, as imports rose in response to strong consumption and investment demand, while export growth declined.

Executive Board Assessment

Executive Directors commended the authorities for their sustained efforts and the success of their economic policies, and for the progress that has been made since the previous Article IV consultation.

Directors welcomed the strong fundamentals in the Canadian economy. The federal government budget now is expected to be balanced no later than the next fiscal year, and all the provincial governments are also expected to balance their budgets by the turn of the century. Determined implementation of monetary policy by the Bank of Canada to achieve its inflation targets has

given Canada one of the lowest inflation rates among major industrial countries. Sound macroeconomic policies have been reflected in a decline in interest rates—to their lowest levels in decades—and improved resource allocation; and the result has been the strong rebound in economic growth and substantial gains in employment over the past year.

Nonetheless, Directors noted, the authorities will face significant new challenges in the period immediately ahead. In particular, monetary policy will have to be managed carefully to ensure that economic growth converges smoothly to its potential path, while taking account of the possible effects of the Asian crisis on the Canadian economy. Fiscal policy will have to ensure that the budget is balanced, as the government has promised, and that the ratio of government debt/GDP is put on a steady downward path. At the same time, the still-high rate of unemployment remains a matter of concern and calls for a strengthening of structural reforms in the labor market.

Directors agreed that more monetary policy restraint had appeared to be called for. The possible effects of the Asian crisis need to be taken into consideration in formulating policy in the period immediately ahead, but the economy continues to exhibit considerable strength, and economic activity is approaching capacity limits. While it was difficult to draw the implications for the stance of monetary policy of the recent widening of the current account deficit and the weakening of the Canadian dollar, Directors expressed understanding of the considerations that had led the Bank of Canada to raise the Bank Rate. More broadly, Directors acknowledged that the economy's productive capacity was not known with a great deal of certainty, and, as the economy approached its estimated capacity limits, it would be appropriate for the authorities to use monetary policy to probe for the actual level of capacity. However, the authorities would need to proceed cautiously, adjusting policy in small steps, with an eye on indications of developing bottlenecks, capacity constraints, and wage pressures. In this way, it could be possible to raise output to a higher level and reduce unemployment to a lower level without triggering a rise in inflation, if structural changes have taken place that raise potential output.

With regard to the inflation target after 1998, Directors generally recommended retention of the current 1–3 percent official inflation target range for the next few years. They noted that continuation of the current target range would allow the economy further time to adjust to a low inflation environment. It would also provide experience in operating monetary policy with inflation targets when the economy is at high rates of resource utilization. In this manner, a better basis would be established for deciding on a longer-term target consistent with the eventual achievement of the objective of price stability. Directors also welcomed the Bank of Canada's approach of basing monetary policy on a number of monetary indicators and not tying them to the mechanical application of the Monetary Conditions Index. Some Directors recommended a timely announcement of the inflation target for 1999 to help reduce any possible uncertainty in the markets about the monetary strategy.

Directors strongly welcomed that policies and fiscal plans now appear to be in place to eliminate fiscal imbalances at both the federal and provincial levels in the period immediately ahead. In these circumstances, the focus of the policy debate has shifted toward the question of how best to use the expected fiscal dividend. Directors noted that there were no easy answers concerning

which path the government should choose for the budget position and the resulting reduction in the ratio of public debt/GDP, particularly in the absence of clear criteria for agreeing on the optimal debt/GDP ratio. Nevertheless, Directors supported the objective of bringing down the debt/GDP ratio more rapidly than would be the case if the budget were maintained in balance. This policy approach could yield many benefits, including reducing the economy's vulnerability to shocks, lowering real interest rates, and helping to address the challenges of an aging population.

Directors also recognized the merit of addressing other priorities, such as efficiency-enhancing tax and spending measures. With respect to using part of the fiscal dividend for purposes other than reducing the debt, they agreed that priority should be given to those tax or spending measures that would enhance efficiency and equity in the economy. They recommended that resources not applied to debt reduction be used primarily to reduce high tax rates and the degree of distortions in the tax system. With regard to additional spending, Directors said that new initiatives should concentrate on reducing poverty traps and other disincentives to work, enhancing equality of opportunity, and improving human capital.

Directors noted that as the provinces put their budgets on sustainable long-term paths, they would need to factor in prospective increases in health care financing requirements as the average age of the population rises. With this in mind, the provinces will need to consider running budget surpluses over the medium term to provide sufficient resources to meet these requirements. The federal government was also likely to be called on to provide additional resources for health care spending, and this possibility should be reflected in its longer-term fiscal plans.

Directors welcomed the recent strong growth in employment, but noted that relatively high rates of unemployment in Canada remained a concern. Expected strong output growth will continue to support employment creation, and recent labor reforms will work to reduce the structural rate of unemployment over time. Nevertheless, Directors considered that further reform of the Employment Insurance (EI) system could help reduce structural unemployment. In particular, they thought that steps could be taken to tighten restrictions on frequent use of the system and to eliminate regional extended benefits. To deal with frequent use, reductions in EI premiums could be tied more closely to the experience with unemployment in individual firms, instead of reducing them across the board.

Directors commended the authorities for their resolve to deal with the critical challenges that the public pension system faces in light of the aging of the population. They noted that measures proposed to restructure existing income supplements and tax credits to senior citizens, and the reforms enacted to address the long-term financing needs of the Canada Pension Plan, would meet these challenges. They encouraged the authorities to act promptly to enact the proposed Seniors Benefit.

Directors noted that progress in implementing measures to reduce internal barriers to trade under the auspices of the Agreement on Internal Trade had been slower than envisaged, and they urged the authorities to push forward with reforms in a timely manner, which would also

contribute to liberalizing the labor market. With respect to international trade, Directors commended Canada's consistent support for free trade. Progress in Canada's unilateral initiative to simplify its tariff system was also commended. However, some Directors recommended further liberalization of trade in agricultural commodities, textiles and clothing, and some service sectors, including the financial sector, which would increase real income and provide welfare gains to Canadian consumers. Directors noted the decline in Canada's official development assistance and, in view of the stronger fiscal position, encouraged the authorities to work toward achieving over time their commitment to the target for foreign assistance of 0.7 percent of GNP.

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Canada: Selected Economic Indicators

	Averages 1960s	1970s	1980s	1992	1993	1994	1995	1996
	(In percent change from previous period at annual rates, unless otherwise indicated)							
Economic activity and prices								
Real GDP	5.6	4.4	2.9	0.9	2.5	3.9	2.2	1.2
Real net exports 1/	0.3	0.0	-0.3	0.4	1.0	0.8	0.9	0.3
Real final domestic demand	5.2	4.6	3.4	1.0	0.5	2.7	0.4	2.0
Consumer spending	4.8	4.5	2.9	1.8	1.9	3.1	1.7	2.4
Nonresidential fixed investment	4.0	5.8	1.4	-15.6	0.5	8.8	-0.7	4.3
Labor force	...	...	2.0	0.5	1.3	1.1	0.7	1.5
Employment	...	...	2.0	-0.6	1.4	2.1	1.6	1.3
Unemployment rate (period average)	...	...	9.4	11.3	11.2	10.4	9.5	9.7
Labor productivity			1.2	1.8	0.9	1.6	0.3	0.4
Capital stock	4.6	4.3	3.7	2.9	2.7	2.8	2.9	3.0
Implicit price deflator for GDP	3.5	8.0	5.8	1.3	1.3	1.2	2.6	1.4
Consumer price index	2.5	7.4	6.5	1.5	1.8	0.2	2.2	1.6
Unit labor cost	...	...	5.6	1.2	0.0	-1.1	1.2	2.3
Nominal effective exchange rate 2/	-1.1	-1.4	-0.1	-5.8	-5.7	-6.2	-2.0	1.7
Real effective exchange rate 3/	...	...	1.9	-6.9	-8.1	-6.8	-3.2	3.6
Exchange rate								
U.S. cents/Canadian dollar	94.4	96.4	79.5	82.4	77.3	73.0	73.1	73.3
Percent change	-1.2	-0.8	-0.1	-5.6	-6.2	-5.6	0.2	0.3
Three-month treasury bill rate	4.8	7.0	11.3	6.6	4.8	5.5	7.0	4.2
Ten-year Treasury bond rate	5.7	8.5	11.7	8.1	7.2	8.4	8.1	7.2
	(In percent of GDP or NDP)							
Balance of payments								
Current account balance	-2.2	-2.6	-2.2	-3.6	-3.9	-2.7	-1.0	0.4
Trade balance	0.9	1.7	2.9	1.3	1.8	2.5	4.2	5.0
Invisible balance	-3.1	-4.3	-5.1	-4.9	-5.7	-5.2	-5.2	-4.6
Real net exports	2.4	2.3	1.3	-0.4	0.6	1.4	2.3	2.5
Fiscal indicators								
General fiscal balance (NIA)	-0.3	-1.0	-4.7	-8.0	-7.5	-5.3	-4.0	-1.7
Federal fiscal balance (NIA)	-0.3	-1.4	-4.6	-4.3	-4.8	-3.4	-3.0	-1.4
Provincial fiscal balance (NIA) 4/	-0.5	-0.7	-0.8	-3.7	-2.6	-1.7	-0.9	0.0
Saving and investment 5/								
Gross national saving	21.9	22.3	20.1	12.6	13.3	15.4	17.6	17.8
General government	4.6	3.1	-1.0	-4.8	-4.7	-2.7	-1.5	0.7
Of which: Federal government	0.6	-0.6	-3.5	-3.5	-4.1	-2.9	-2.6	-1.0
Private	17.3	19.2	21.1	17.5	18.0	18.1	19.1	17.2
Personal	7.0	9.8	11.9	10.8	9.9	8.3	8.1	6.9
Business	10.3	9.4	9.2	6.7	8.1	9.7	10.9	10.3
Gross domestic investment	23.5	23.6	21.4	17.2	17.4	18.4	18.0	17.3
Private	18.9	20.0	18.6	14.6	14.8	15.7	15.4	15.0
Public	4.6	3.6	2.8	2.7	2.5	2.6	2.5	2.3
Of which: Federal government	0.7	0.5	0.5	0.5	0.5	0.5	0.5	0.4
Net foreign investment	1.8	1.8	1.9	5.6	4.9	3.7	0.7	-0.8
Net national saving	13.5	14.3	10.8	0.4	1.2	3.9	6.7	6.7
Net private investment	12.1	14.0	11.6	5.6	5.9	7.1	6.5	5.5
In real terms								
Gross domestic investment	15.4	15.7	17.6	17.2	17.3	18.1	17.9	17.6
Private	12.3	13.3	15.5	14.6	14.7	15.5	15.3	15.2
Public	3.1	2.4	2.1	2.7	2.6	2.7	2.6	2.4

Sources: Statistics Canada; and IMF staff estimates.

1/ Contribution to growth.
2/ Constructed using 1989–91 trade weights.
3/ Defined in terms of relative normalized unit labor costs in manufacturing, as estimated by the IMF's Competitiveness Indicators System, using 1989–91 trade weights.
4/ Includes local governments.
5/ Gross domestic investment does not equal the sum of gross national saving and net foreign investment because of statistical discrepancy.

Press Information Notice (PIN) No. 98/15
FOR IMMEDIATE RELEASE
March 10, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Cape Verde

The IMF Executive Board on February 20, 1998 concluded the 1998 Article IV consultation[1] with Cape Verde.

Background

In recent years, the government of Cape Verde has pursed an economic reform program aimed at reducing the size of the public sector and boosting economic growth by increasing the country's export base. The accomplishments to date include (1) liberalization of most imports and prices; (2) reform of the tax system and improvements in tax administration; (3) an initial restructuring of the financial sector; and (4) privatization or liquidation of 14 important public enterprises. Although real GDP growth rose to an annual average rate of above 4 percent during the period 1992–95, unemployment remained at about 25 percent of the active population. Given the small, open economy of Cape Verde, the authorities maintained a nominal exchange rate peg to control inflation. Despite important efforts at structural reform, lax government fiscal policies during 1992–95 led to a rapid increase in public spending, an accumulation of domestic debt, and the virtual depletion of foreign exchange reserves in early 1996.

In response, the authorities tightened financial policies, and imposed import controls on 26 products in mid-1996. As a result, there was some progress in redressing macroeconomic imbalances, and the stock of international reserves began to increase; however, the economic situation remained fragile. The overall government deficit, on a commitment basis, narrowed from a peak of 16.1 percent of GDP in 1996 to 15.1 percent in 1997. Privatization receipts financed

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

most of the deficit in 1996, while in 1997 the deficit was financed by recourse to domestic bank financing. This brought the stock of domestic debt to C.V. Esc 18.2 billion, or about 46 percent of GDP, at end-1997. Reflecting a persistent drought, real GDP growth was only 3 percent per year in 1996 and 1997. Inflationary pressures persisted, with an annual inflation rate of 9 percent during these years.

A tight credit policy was pursued during 1996 in support of a fixed nominal exchange rate and with the objective of rebuilding foreign exchange reserves; overall domestic bank credit increased by only 10 percent. In 1997, however, domestic bank credit rose by an estimated 20 percent because of a large expansion of credit to government. As a result, the exchange rate came under pressure and foreign exchange reserves began to decline.

The external current account deficit, including grants, narrowed by about 6 percentage points of GDP in 1996 to just under 7 percent, but widened slightly in 1997. Exports continued to grow rapidly, albeit from a small base, but the capital and financial account weakened, reflecting the strengthening of the commercial banks' external position as the government deposited foreign exchange privatization proceeds in commercial banks. The quantitative import restrictions imposed in 1996 were lifted in November 1997.

The authorities made significant progress in several areas of a structural reform during 1996 and 1997. They accelerated the privatization program and made efforts to strengthen expenditure management. In addition, the government launched in 1997 a civil service voluntary departure scheme, which will enter into full operation in 1998.

Beginning in 1998, the authorities, with the support of the donor community, will undertake a major domestic debt reduction operation. To underpin this effort, Cape Verde has requested a stand-by arrangement with the IMF, which will provide the authorities and donors the means by which to gauge the country's progress in implementing its macroeconomic program. The authorities have indicated that they do not intend to draw on this arrangement. The budget adopted for 1998 calls for a reduction of the overall deficit to less than 9 percent of GDP in 1998, which is to be entirely financed by concessional foreign borrowing. Total expenditure is programmed to decline from an estimated 54 percent of GDP in 1997 to 50 percent in 1998, with most of the reduction coming from a decline in interest payments and cuts in domestically financed capital expenditure. These expenditure reductions will be supported by administrative measures to strengthen budgetary execution.

Executive Board Assessment

Directors welcomed the authorities' continued efforts in implementing structural reform and economic liberalization measures since 1992. However, Directors emphasized that such measures would be effective in providing a basis for sustainable growth only if they were accompanied by persistent sound financial policies aimed at restoring macroeconomic stability. Directors welcomed the renewed impetus given to these efforts to strengthen structural reforms and improve the climate for private sector growth. They supported the pursuit of these policies in the context of a IMF arrangement.

Directors welcomed the reduction in the overall fiscal deficit envisaged in the government budget for 1998. In their view, this was a key element of Cape Verde's economic program. They cautioned that close monitoring of the budget would be necessary to ensure its successful implementation, and urged the authorities to put in place in the near future administrative reforms aimed at improving budgetary control. Directors noted that the recovery of debt from public enterprises represented an important part of the fiscal improvement expected in 1998 and thus needed to be pursued forcefully. In future years, stronger efforts would be needed to reduce current government expenditure, especially the wage bill. Directors welcomed the domestic debt reduction operation being supported by Cape Verde's donors.

Directors observed that the openness of the Cape Verdean economy, its dependence on emigrant remittances, and the underdeveloped tools of monetary policy available to the central bank suggested that a nominal exchange rate peg would continue to provide an appropriate nominal anchor. However, they stressed the need for the authorities to pursue strong fiscal and monetary policies in order to ensure the sustainability of the exchange rate.

Directors emphasized the importance of accelerating the ongoing structural reform program to foster sustained economic growth. They also underscored the urgent need for improvements in Cape Verde's statistical system.

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Cape Verde: Selected Economic Indicators, 1994-98

	1994	1995	1996	1997	1998 Program
			(In percent)		
Domestic economy					
Change in real GDP	3.8	4.7	3.0	3.0	4.0
Change in consumer prices (end of period)	4.1	5.6	9.1	8.9	3.5
			(In millions of U.S. dollars) 1/		
External economy					
Exports, f.o.b.	19	25	28	37	46
Imports, f.o.b.	195	234	206	209	232
Current account balance 2/	-43	-54	-29	-33	-30
Direct investment and project grants	23	47	41	22	47
Capital account balance	36	78	28	36	42
Current account balance (percent of GDP) 2/	-12.3	-12.9	-6.7	-7.7	-6.4
Change in real effective exchange rate (in percent)	-2.7	2.3	-1.3	4.2	...
			(In percent of GDP) 1/		
Financial variables					
Gross national savings	33.1	27.4	28.3	25.8	28.4
Gross domestic investment	45.4	40.3	35.0	33.4	34.9
Central government balance	-16.5	-15.1	-16.1	-15.1	-8.7
Primary balance	-33.4	-28.8	-26.5	-23.5	-19.1
Change in broad money (in percent)	16.3	20.6	9.9	7.7	...

Source: Data provided by the Cape Verdean authorities; and IMF staff estimates.
1/ Unless otherwise indicated.
2/ Including grants.

Press Information Notice (PIN) No. 98/8
FOR IMMEDIATE RELEASE
February 20, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Chile

The IMF Executive Board on February 11, 1998 concluded the 1997 Article IV consultation[1] with Chile.

Background

Chile's performance since the beginning of the decade has been remarkably strong. Through a combination of prudent fiscal and credit policies, stringent financial sector supervision, structural reforms, an open trade and investment regime, and efforts to improve social conditions, the country has achieved rapid output growth with a reduction in poverty, declining inflation, and a solid external position. Real GDP growth averaged 6.8 percent from 1990 to 1997, inflation declined from 27.3 percent to 6 percent during the period, official foreign reserves amounted to US$17.4 billion at end-1997 (close to ten months of imports of goods and nonfactor services), and the incidence of poverty fell from nearly two-fifths of the population in 1990 to less than one-fourth in 1996.

Economic management was complicated in recent years by sharp swings in export prices—especially copper. After a surge in 1995, the price of copper declined by over 20 percent in 1996, recovered in early 1997, and fell sharply later in the year, contributing to sharp fluctuations in the trade and fiscal balances. To limit the impact of these movements on demand and output growth, the authorities have periodically adjusted the overnight real interest rate, the central bank's main instrument of monetary control, while trying to keep the fiscal stimulus to the economy broadly neutral. Lower copper export prices also contributed to a decline in the nonfinancial public sector

[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

surplus—from 3.5 percent of GDP in 1995 to about 2 percent in 1996 and the first half of 1997 (the latest data available). However, the cyclically adjusted fiscal stance remained broadly neutral in terms of its stimulus to the economy, as an expansion in the coverage of social programs aimed at alleviating poverty and reducing income disparities, including through increases in minimum pensions and an ambitious education reform, was mostly financed through matching tax increases. Output growth is estimated to have slowed from 7¼ percent in 1996 to 6½ percent in 1997.

The task of disinflation in 1996-97 was complicated by a number of other supply shocks (mostly weather related) that contributed to temporary but significant hikes in food and energy prices. Nonetheless, inflation declined to 6.6 percent at end-1996 and 6 percent at end-1997, in line with the authorities' targets.

Reflecting the decline in copper export prices, the country's external current account position shifted from a small surplus in 1995 to a deficit of about 4 percent of GDP in 1996-97. Rising profit remittances, reflecting strong foreign direct investment flows since the early 1990s, also helped widen the deficit. The financing of the current account deficit in recent years has shifted from debt to sizable inflows of direct and, to a lesser extent, long-term portfolio investment. Overall, large capital inflows contributed—up to the last quarter of 1997—to a gradual but steady real effective appreciation of the currency. The authorities have continued to deal with these pressures through a combination of prudential fee-based restrictions on inflows aimed at discouraging short-term foreign borrowing, a progressive liberalization of outflows (the existing prudential regulations apply mainly to foreign investment by financial institutions), and occasional discrete changes in the exchange band (including a revaluation in January 1997). In the aftermath of the crisis in Asia, the peso has come under some pressure, weakening by about 8 percent in nominal terms against the U.S. dollar since mid-October 1997. However, the authorities have averted an overshooting of the exchange rate through a tightening in credit conditions, moderate foreign exchange intervention, and cuts in public expenditure.

There have been important further advances in the area of structural reforms in recent years, with the approval of bills increasing private sector participation in the upgrading of infrastructure, as well as improving governance (particularly in the judicial area) and social equity (including through the above mentioned education reform). The supervisory and regulatory framework for the financial system has been updated and strengthened. Overall, bank performance indicators have improved throughout the 1990s along with a process of modernization (including higher foreign investment in the sector) and continued financial deepening.

Executive Board Assessment

Executive Directors noted that Chile had a long record of prudent and skillful economic management, and that recent policies and structural reforms had delivered a very good economic performance in 1997. The strong output growth, the decline in underlying inflation, and a sizable buildup in foreign reserves had created the conditions for further sustained gains in living standards, and had also served to strengthen policy credibility.

Directors considered that Chile's sound fundamentals, as well as its favorable debt and debt-service indicators, robust financial system, and ample cushion of foreign reserves had equipped it to deal relatively well with the recent turbulence in world financial markets. In this context, they noted the authorities' prompt actions to tighten monetary policy when the peso came under

pressure. However, Directors cautioned that the country's vulnerability to the events in Asia, particularly given the importance of its exports to that region, as well as the prospects of a prolonged sluggishness in commodity prices and a possible slowdown in capital flows to emerging markets, required vigilance on the part of the authorities and a readiness to tighten macroeconomic policies, if needed. Some Directors saw scope for a rebalancing of the policy mix, with some strengthening of fiscal policy. However, several other Directors considered that reliance on tight monetary policy was appropriate for the time being, especially given the recent exchange rate depreciation and the relative strength of the banking system, which could well withstand the effects of higher interest rates. They also agreed that continued unrestricted access to industrial country markets was crucial to solidify Chile's outward-looking orientation.

Directors considered that Chile's prudential restrictions on external indebtedness in the form of a one-year nonremunerated deposit requirement had played a useful role in reducing the volatility of capital inflows and in lengthening the maturity of external obligations. They noted the prudential character of these regulations, and the fact that they operated alongside a stringent system of financial supervision. Some speakers noted that their usefulness in the Chilean case may reflect importantly the country's strong fundamentals and progress in restructuring the economy. They also felt that such restrictions tend to lose effectiveness over time.

Directors were encouraged by the authorities' determination to slow the increase in consumer prices to around 4.5 percent in 1998, building on the central bank's credibility in successfully lowering inflation since the beginning of the decade. They welcomed the recent steps to tighten credit, cut certain public outlays, and cushion the depreciation of the currency through moderate foreign exchange intervention. In their view, however, the risks to the external outlook heightened the importance of measures to reduce the country's reliance on foreign savings, including the maintenance of a strong fiscal position over the short and medium term. In this regard, Directors noted the importance of raising private savings, and welcomed the authorities' decision to examine potential measures to this end, through the imminent publication of the report of the commission that is reviewing ways to bolster private savings.

Directors commended the authorities on the impressive progress made in structural reforms, including the recent measures to significantly strengthen the banking system, undertake reforms in education, and improve the judicial system. Directors endorsed warmly the authorities' plans to deepen structural reforms with a view to diversifying the economy and reducing the economy's vulnerability to external shocks, achieving further productivity gains, as well as further improving social conditions. Directors also welcomed government plans to further reform financial sector regulations, especially by introducing consolidated supervision of financial holding groups; upgrade infrastructure with an increased private sector role; improve the quality of education and other basic services; and strengthen the regulatory framework for public utilities. In addition, they welcomed the government's initiative to seek increased transparency in its own military outlays and those in the rest of the region.

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Chile: Selected Economic Indicators

	1993	1994	1995	1996	Prel. 1997
			In percent		
Domestic economy					
Change in real GDP	6.3	4.2	8.5	7.2	6.5-6.7
Unemployment rate	6.5	7.8	7.4	6.5	6.1
Change in consumer prices (end of period)	12.2	8.9	8.2	6.6	6.0
			In million of U.S. dollars 1/		
External economy					
Exports, f.o.b.	9,199	11,604	16,136	15,353	16,875
Imports, f.o.b.	10,181	10,879	14,655	16,500	18,218
Current account balance	-2,077	-639	147	-2,918	-3,182
Direct investment	429	950	1,185	3,094	2,532
Portfolio investment	729	908	36	1,101	2,379
Capital account balance	2,653	3,833	914	4,099	5,654
Gross official reserves 2/	9,225	12,893	14,241	14,915	17,386
Current account balance (in percent of GDP)	-4.5	-1.2	0.2	-4.1	-4.0
Change in real effective exchange rate (in percent) 3/	0.4	5.8	1.7	3.9	9.4
			In percent of GDP 1/		
Financial variables					
Nonfinancial public sector balance	1.8	2.2	3.5	2.0	1.8
Combined public sector balance	0.8	1.2	3.0	1.3	1.2
Change in broad money (M3)	27.0	19.3	27.4	22.0	19.0
Interest rate 4/	6.5	6.4	6.1	7.3	6.8
External debt	47.8	46.8	36.5	34.4	33.2
Copper price (U.S. cents per pound)	86.7	104.9	133.2	103.2	103.2

Sources: Data provided by the Chilean authorities; and IMF staff estimates.

1/ Unless otherwise indicated.
2/ Gold valued at US$42.22 per ounce.
3/ Percentage change for the 12 months ended December; a decline indicates a depreciation of the Chilean peso.
4/ In percent over monetary correction; 90-day central bank paper.

Press Information Notice (PIN) No. 98/12
FOR IMMEDIATE RELEASE
March 6, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with the Czech Republic

The IMF Executive Board on February 13, 1998 concluded the 1997 Article IV consultation[1] with the Czech Republic.

Background

After achieving early and decisive progress in stabilization and structural reform, the Czech Republic has experienced large macroeconomic imbalances in the last few years. Huge capital inflows in 1994-95 complicated monetary management under a fixed exchange rate regime and stimulated domestic demand, while weak corporate governance fueled wage growth. As a result, the current account deficit widened sharply, to 7½ percent of GDP in 1996, and the rate of inflation exceeded that in the Czech Republic's main trading partners. Real GDP growth picked up to nearly 6 percent in 1995, but slowed to about 4 percent in 1996.

Notwithstanding a tightening of monetary policy from mid-1996, the current account imbalance widened further in early 1997 owing to high wage growth, lack of fiscal support, and a nominal appreciation of the koruna within the exchange rate band. As a result of the market's reassessment of the fundamentals and contagion effects from Thailand, in May 1997 speculative pressures against the koruna led to the adoption of a managed float and a depreciation to 10-12 percent below the former central parity. In the second half of the year, fiscal and monetary tightening, increased exchange rate flexibility and strengthened foreign demand all contributed to restoring order in the foreign exchange market and to a narrowing of the external deficit. Nevertheless, political uncertainty and contagion effects from the East Asian currency crises

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

contributed to further depreciation pressures in the last quarter of 1997; this prompted temporary increases in interest rates and intervention in the foreign exchange market by the Czech National Bank (CNB). More recently, the market has reacted relatively favorably to the appointment of a new cabinet, while the intensification of the Asian crisis has had little effect on the Czech Republic.

The current account deficit narrowed to 6–6½ percent of GDP in 1997, with all of the improvement concentrated in the second half of the year when the deficit was about 5 percent of GDP. After five quarters of sluggish export performance, exports began to grow rapidly from the second quarter of 1997, mainly reflecting the recovery of economic activity in western Europe, the sharp deceleration of domestic demand, and the beneficial effect of previous foreign direct investment. The growth of imports decelerated sharply. The capital account is estimated to have recorded a surplus of 3 percent of GDP in 1997; of this, one half was in the form of nondebt capital inflows. Total gross external debt was US$22 billion at end-1997, equivalent to about 40 percent of GDP. The debt service ratio remains relatively low and the Czech Republic enjoys an investment grade sovereign rating by foreign agencies. Official reserves amounted to US$9¾ billion at end-1997, equivalent to 4½ months of merchandise imports.

Developments in the domestic economy were on the whole disappointing in 1997. A steep decline in investment kept real GDP growth to 1–1½ percent despite the strength of exports. Consumption also weakened in the second half of 1997. Extensive floods in July caused physical damage valued at 4 percent of GDP and lowered output growth by ½ percentage point. Unemployment rose from 3½ percent at end-1996 to 5¼ percent at end-1997. Inflation reached 10 percent in the 12 months to end-1997, up 1½ percentage points from the previous year; this reflected larger increases in administered prices. Nominal wage growth decelerated significantly but remained high in relation to productivity gains.

Fiscal and monetary tightening were key to the improvement in the external position. The general government deficit was contained to about 2 percent of GDP in 1997, compared with a deficit of 1¼ percent of GDP in 1996, notwithstanding the impact of floods (about 1¼ percent of GDP) and lower than expected economic activity. This was made possible by expenditure cuts of 2½ percent of GDP, announced in April-May. Broad money growth was kept within or below the 7–11 percent target range throughout 1997—down from almost 20 percent in mid-1996. Interest rates have trended upward since April 1997.

The pace of enterprise restructuring and financial sector reform has been sluggish in recent years. As a consequence of voucher privatization in 1991–94, diffuse ownership and residual state shareholdings have preserved a controlling state interest in major enterprises and banks, and progress toward effective privatization of these entities has been relatively slow. The resulting weak corporate governance has contributed to rapid real wage growth. Furthermore, sluggish economic activity and relatively high real lending rates have adversely affected the financial position of banks. The central bank has been involved in restructuring of the small banks over the past few years through mergers, liquidations and capital injections to clean up portfolios. The government recently reached agreement on the sale of the state's remaining share in one of the four major banks, and technical preparations are underway for the sale of the state's stake in the other three major banks.

Executive Board Assessment

Executive Directors commended the authorities for their determined response to the major challenges they had faced in mid-1997—namely, a large external imbalance and disorderly conditions in the foreign exchange market, owing in part to spillover effects from the East Asian currency crises. They noted that monetary and fiscal tightening, and the timely adoption of a managed float, were key to the subsequent narrowing of the current account deficit and the return of relative stability in the foreign exchange market. However, Directors observed that the costs had been high—unavoidably so given the size of the external imbalance—as evidenced by a steep decline in investment and growth, and a rise in unemployment. Noting that the external position remained fragile and inflation high, Directors stressed the need to maintain tight financial policies and to implement a much more vigorous approach to wage discipline. Restructuring of enterprises and addressing weaknesses in the banking system were also seen as essential for setting the stage for renewed growth in a noninflationary environment.

Directors welcomed the authorities' objectives of reducing the external imbalance and the rate of inflation in 1998 through a further deceleration of nominal wage growth, continued tight macroeconomic policies, and accelerated structural reform. Against the background of a still large current account deficit and a vulnerable external position, Directors stressed the importance of adhering strictly to announced policy intentions in order to sustain adjustment and strengthen market confidence, and in view of the upcoming elections, they emphasized the need for any future government to continue the policies and structural reforms now underway.

Directors agreed that wage restraint was key to the continued adjustment. They noted that, while wage growth had slowed significantly in 1997, this was due mainly to strict limits on wage increases in the budget. Wage growth in the rest of the economy, albeit decelerating, was still high, owing in large part to developments in state-controlled enterprises. They welcomed, therefore, the authorities' intention to reduce nominal wage growth in state-controlled enterprises sharply in 1998, which could have a favorable demonstration effect on other sectors. They also noted, however, that wage discipline could only be lastingly addressed through structural reform, notably completion of the divestment of state-controlled enterprises. A few Directors proposed a more comprehensive incomes policy to encompass the private sector. These Directors suggested that the government, in consultation with the private sector, consider setting general wage guidelines as a guide to wage bargaining at a decentralized level. Other Directors, however, thought that such an incomes policy would reintroduce rigidities in the wage bargaining system without addressing the root cause of wage pressures, which was weak corporate governance.

Directors generally stressed the continuing need for a tight fiscal policy stance in support of the stabilization effort. They commended the authorities for the sizeable expenditure cuts announced in April-May 1997 in response to depreciation pressures on the koruna. As a result of these measures, it had been possible to contain the fiscal deficit in 1997 despite lower than expected economic activity and the sizeable impact of flood-related expenditures in July. Directors also welcomed the authorities' plans to reduce the general government deficit to 1 percent of GDP in 1998. However, Directors were concerned that the authorities' revenues and expenditures projections may be too optimistic and that further fiscal measures could be needed to achieve these targets. In this regard, they welcomed the authorities' intention to take additional measures

as needed during the year. A number of Directors encouraged the authorities to aim at achieving a small budget surplus over the medium term, particularly if wage growth turned out to be higher than envisaged and external adjustment showed signs of slowing.

Directors commended the CNB for its handling of the currency crisis through determined use of interest rate policy and increased exchange rate flexibility. The CNB's policies had been successful in stabilizing the exchange rate at an acceptable level without imposing undue burdens on the banking and enterprise sectors. Directors stressed that the vulnerability of the external position and the persistence of inflation meant that monetary policy would have to remain restrictive. Indeed, they noted that the CNB should stand ready to increase interest rates to support the exchange rate and the stabilization effort. In this regard, Directors observed that in the current environment there was no apparent conflict between the inflation and the external current account objectives. Many Directors, therefore, agreed on the potential benefits, in terms of guiding policies and signaling the market, of the new monetary policy framework based on inflation targeting. However, a few Directors questioned whether inflation targeting was appropriate at this stage of development of the economy. While Directors generally agreed that, were a conflict to arise between objectives, the CNB should assign priority to the external objective, some argued that this could put the inflation targeting mechanism and its benefits in doubt.

Directors were concerned about the condition of the banking system, given the large share of nonperforming loans and the effects of tight financial policies and the economic downturn on bank profitability. They stressed the need to monitor the banks closely; this would require additional resources devoted to bank supervision and more frequent on-site inspections. They also encouraged the timely passage of legislation to ease the foreclosure process and improve the tax treatment of provisioning. Directors welcomed the efforts to restructure the small banks, the plans to privatize the large state-controlled banks, and the recent measures to strengthen the legal and regulatory framework. They urged the authorities to follow through on these plans and to reinvigorate their efforts to strengthen the financial position of the banks.

Regarding structural reform, Directors regretted the continued delays in the privatization process, and urged the authorities to accelerate privatization in order to improve corporate governance and foster the restructuring of the economy. They welcomed recent measures to promote reform of the capital market, including the establishment of a Securities and Exchange Commission, but cautioned that it would take time to improve the functioning of the market and strengthen investor confidence. The need to ensure the long-term viability of the pension system through appropriate reforms was also mentioned.

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Czech Republic: Selected Economic and Financial Indicators

	1993	1994	1995	1996	1997 Est.
			(Change in percent)		
Real Economy					
Real GDP	0.6	2.7	5.9	4.1	1-1½
Consumer prices					
Period average	20.8	10.0	9.1	8.8	8.4
End-period	18.2	10.2	7.9	8.6	10.0
Unemployment rate (end of period)	3.5	3.2	2.9	3.5	5.2
Gross national savings (in percent of GDP) 1/	29.5	27.4	29.0	25.4	23.9
Gross domestic investment (in percent of GDP)	28.0	29.3	32.5	33.0	30.2
			(In percent of GDP)		
Public Finance 2/					
Revenues	46.7	46.4	45.0	42.9	41.1
Expenditures	45.4	46.0	45.7	43.9	42.8
Deficit (-)	0.5	-1.2	-1.8	-1.2	-2.1
Gross debt (central government)	15.8	13.8	11.5	10.2	10.9
	(12-month change in percent of beginning of period broad money)				
Money and Credit (end of period)					
Broad money	19.8	19.9	19.8	9.2	7.9
Credit to enterprises and households	18.9	16.6	12.7	9.9	9.4
Net foreign assets	9.5	11.2	10.6	-1.7	6.2
			(In percent)		
Interest Rates (average) 3/					
Lending rate	14.0	12.8	12.7	12.0	13.2
Deposit rate	6.9	6.9	6.9	6.7	7.7
			(US$ billions)		
Balance of Payments					
Trade balance	-0.5	-1.3	-3.7	-5.9	-4.4
Current account	0.5	-0.7	-1.4	-4.3	-3.3
(Percent of GDP)	1.5	-1.9	-2.7	-7.6	-6.3
Gross official reserves (end of period)	3.9	6.2	14.0	12.4	9.8
Reserve cover (months of merchandize imports)	3.2	4.3	6.7	5.4	4.4
External Debt, end of period					
External debt in convertible currencies	8.5	10.7	16.5	20.8	21.8
			(SDR millions)		
Fund Position					
Quota					589.6
Fund holdings of currency					589.6
(In percent of quota)					100.0
Exchange Rate					
Exchange rate regime:	Currently a managed float; until May 27, 1997, pegged to a DM/US$ basket with fluctuation margins				
Present rate (February 13, 1998)	CZK 34.636 = US$1				
Nominal exchange rate against the currency basket 4/	1.004	1.005	1.004	1.014	0.952
Real effective exchange rate 5/ (CPI-based, Jan.-Sep. 1990=100)	110.5	118.0	124.8	134.6	133.2

Sources: Data provided by the Czech authorities; and IMF staff estimates.
1/ Includes statistical discrepancy (in contrast to official statistics which include the discrepancy in domestic investment).
2/ Includes central government, local authorities and social insurance funds. Excludes privatization revenues equivalent to 0.8 percent of GDP in 1993, 1.6 percent of GDP in 1994, 1.1 percent of GDP in 1995, 0.2 percent of GDP in 1996, and 0.4 percent of GDP in 1997.
3/ Average rate in last quarter.
4/ The currency basket comprises the Deutsche mark (weight of 65 percent) and the U.S. dollar (weight of 35 percent).
5/ 1997 figure refers to January-September.

Press Information Notice (PIN) No. 98/26
FOR IMMEDIATE RELEASE
April 6, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with El Salvador

The IMF Executive Board on February 20, 1998 concluded the 1997 Article IV consultation[1] with El Salvador.

Background

Economic activity continued the recovery initiated in late 1996, and real GDP growth accelerated to 3.8 percent in 1997 from 2 percent in 1996 led mainly by a strong rebound in exports and continued growth of the financial sector, while activity in the construction sector expanded on account of low income housing. At the same time, inflation declined to 1.9 percent during 1997 from 7.4 percent a year earlier helped by a prudent monetary policy, falling international prices of oil and cereals, and the appreciation of the dollar to which the colón is pegged. The external current account position continued to strengthen in 1997 as coffee exports grew by about 50 percent (26 percent increase in prices and 18 percent in volume). Also, nontraditional exports grew by 20 percent (5 percent in 1996) reflecting both a recovery of the Central American market and penetration of new markets niches. The sharp deceleration of inflation during 1997 to below that of the trading partners for the first time in the 1990s contributed to slow down the real effective appreciation of the colón stemming from the appreciation of the U.S. dollar.

The fiscal position also improved in 1997, with the overall public sector deficit (before grants) declining to 2 percent of GDP from 2.6 percent the previous year. The public finances were affected negatively in 1997 by a significant shortfall in tax revenue despite further efforts in tax administration. In response, the authorities took steps to enhance VAT collections, cut public

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

expenditure, including by maintaining the freeze on public sector wages for the second consecutive year and postponing transfers and capital outlays to 1998, and tightened monetary policy.

The financial system was affected by the spillover from the collapse in July 1997 of two small financial institutions. To bolster confidence, and also to sterilize the increase in foreign exchange reserves, the central bank contained the reduction in the interest rates to significantly less than the drop in inflation. At the same time, however, growth of credit to the private sector accelerated during 1997 (to 15.5 percent in real terms from 7.6 percent during 1996), while broad money expanded in real terms at a somewhat faster pace than in 1996.

Progress was made in 1997 on structural reforms, including the modernization of the public sector, reduction of import duties, environmental policy, and an innovative community-managed school program. Also, the superintendency of pensions became operative in June 1997, with private managers of individual accounts expected to start operations by June 1998. Four electricity distribution companies were privatized in January 1998, and the privatization of the telephone company is underway with the sale to be completed by June 1998.

Executive Board Assessment

Executive Directors were in agreement with the thrust of the staff appraisal. They noted that in 1997 the pace of economic activity accelerated significantly, inflation fell below that of trading partners, and the external current account strengthened further, mainly owing to a sharp recovery of nontraditional exports and maquila, and a large gain in the terms of trade on account of coffee prices. However, the fiscal position improved less than had been envisaged in the program mainly because of a shortfall in tax revenues. Moreover, the structural reform process slowed down, reflecting delays in the privatization of the telephone company (ANTEL) and in the implementation of the pension reform.

Directors welcomed the authorities' prompt and decisive response to the shortfalls in revenue in 1997 by curtailing and postponing expenditure, and tightening monetary policy. These actions were particularly commendable, given the political pressures faced by the government to loosen policies before and following the elections, and in view of the difficulties experienced by the financial system. Directors welcomed the authorities' intention to maintain financial discipline, and they supported the request for the extension and rephasing of the Stand-By Arrangement to May 30, 1998.

Directors underscored the need to keep public finances under control in 1998, while maintaining a monetary policy that would slow the rapid credit expansion to the private sector. Directors welcomed the authorities' efforts to improve tax collections and their commitment to tighten fiscal targets under the program if additional revenues were to materialize. The need to address the issue of declining tax revenues stemming from the reduction in import duties with a view to achieving a sustainable fiscal position over the medium term was also underscored by Directors.

Directors welcomed the resumption of privatization of public utilities, which will contribute to increasing productivity and strengthening external competitiveness, while increasing the country's exposure to investment opportunities by foreign investors. Directors noted that pressures to spend a larger portion of the privatization proceeds than envisaged in the program for 1998 should be resisted so as not to put pressure on domestic prices; this is essential to preventing a further loss of competitiveness and, consequently, to sustaining higher rates of growth. In this context, they supported the authorities' decision to use a large part of the larger-than-expected proceeds from the sale of the electricity distribution companies to repay the outstanding external short-term debt, and to create a special investment fund with the remainder of the proceeds, including from the sale of ANTEL, to finance investment outlays over a three-year period.

Directors welcomed the authorities' initiative to strengthen banking supervision, and welcomed the decision to improve the operation of indirect instruments of monetary control.

While Directors noted that the exchange rate peg had supported the authorities' stabilization efforts, they emphasized the importance of monitoring closely the impact of the exchange rate on the external position.

It is expected that the next Article IV consultation with El Salvador will be held on the standard 12-month cycle.

Press Information Notices (PINs) are issued, at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

El Salvador: Selected Economic Indicators

	1994	1995	1996	Prel. 1997	Prog. 1998
	(Annual percentage changes; unless otherwise specified)				
Output and prices					
Real GDP	6.0	6.3	2.1	3.8	4.0
Consumer prices (end-of-period)	8.9	11.4	7.4	1.9	3.5
Unemployment rate (in percent of the labor force)	7.7	7.7	7.7	7.8	...
Real effective exchange rate (depreciation -)	1.7	7.7	5.0	4.5	...
Interest rate (180-day deposits, in percent)	13.0	16.4	12.0	12.7	...
Money and credit 1/					
Net domestic assets of the financial system	17.5	16.5	14.4	8.0	3.4
Credit to the private sector	16.3	23.3	13.1	15.5	10.9
Liabilities to the private sector	18.3	12.7	17.3	12.3	12.3
	(In percent of GDP; unless otherwise specified)				
Nonfinancial public sector					
Nonfinancial public sector balance after grants (deficit -)	-0.6	-0.1	-2.4	-1.8	-3.0
Central government	-0.8	-0.5	-2.0	-1.2	-2.2
Public enterprises	-0.1	0.0	-0.6	-0.8	-0.7
Social Security Agency	0.3	0.3	0.2	0.1	0.1
Savings and investment					
Gross domestic investment	19.8	20.3	16.2	16.2	17.3
Private sector	15.8	15.0	12.3	12.6	13.2
Public sector	4.0	5.3	3.9	3.6	4.1
Gross national savings	16.1	15.5	14.0	15.1	15.1
Private sector	14.1	12.3	12.2	13.5	13.9
Public sector	2.0	3.2	1.8	1.6	1.2
External current account before grants (deficit -)	-3.7	-4.8	-2.2	-1.1	-2.2
External sector					
Overall balance of payments (in millions of U.S. dollars)	143	147	165	362	410
Gross international reserves (in millions of U.S. dollars)	788	935	1,099	1,461	1,871
(in months of imports)	4.2	3.9	4.9	5.9	7.0
External public debt	25.6	23.7	24.4	24.4	20.9

Sources: Ministry of Finance; Central Reserve Bank; and IMF staff estimates and projections.

1/ In relation to liabilities of the financial system to the private sector at the beginning of the period.

Press Information Notice (PIN) No. 98/32
FOR IMMEDIATE RELEASE
April 29, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Guinea

The IMF Executive Board on April 3, 1998 concluded the 1998 Article IV consultation[1] with Guinea at the same time it approved the authorities' request for financial support under the Enhanced Structural Adjustment Facility (see Press Release No.98/11).

Background

Guinea made important progress during 1997 in its efforts to consolidate and advance economic reforms that were launched in the latter part of 1996, and are being supported by the IMF under a three-year ESAF loan approved in early January 1997. Real GDP is estimated to have grown by 4.7 percent, spurred by increased activity in agriculture, trade, and construction. Inflation continued to abate, from an average rate of 3 percent in 1996 to 1.9 percent in 1997. However, inflation picked up at the end of the year to a 12-month rate of 5.2 percent in December, as higher demand associated with the holiday period was accomodated by a stronger-than-progammed expansion in broad money during the year.

The fiscal situation also improved, as total budget revenue increased to 11 percent of GDP from 10 percent in 1996, benefitting in particular from the full-year impact of the value-added tax, and increased collection efforts. The domestic primary budget surplus (revenue minus noninterest domestic expenditure) rose by 1½ points to 2.8 percent of GDP, as domestic primary expenditure was cut back under strict cash management. This improved fiscal position, together with a sizable pick-up in external financing inflows, allowed the authorities to reduce domestic and external payments arrears along with debt to the domestic banking system.

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

Broad money expanded by 17.3 percent during the year, much more than nominal GDP, reflecting higher-than-expected credit to government and net foreign assets. Nevertheless, bank credit to the private sector fell below its end-1996 level, most likely because of the banks' reluctance to lend to the private sector in view of the continuing difficulties in enforcing loan contracts before the courts. The reference interest rates for the economy, a minimum deposit rate and a maximum lending rate, remained unchanged during the year.

Guinea's external current account deficit was unchanged from 1996 at close to 8 percent of GDP despite an improvement in the trade balance of about 1 percent of GDP attributable to a broad-based recovery in exports. Meanwhile, the resumption in program assistance led to an important surplus in the capital account that permitted gross official reserves to rise to the equivalent of three months of imports. During 1997, Guinea reduced its external arrears, benefiting from a debt rescheduling by Paris Club creditors and the conversion of its debt to the former Czechoslovakia.

The structural reform in 1997 was dominated by actions to address the difficulties of several ailing banks, and the closure of one bank (the BIAG) in November 1997. The liquidation of the BIAG has been orderly, and at end-December 1997, most of the small depositors had been reimbursed, while the large ones had received a base amount in cash, with the remainder being repaid with government securities. The rehabilitation of the National Social Security Fund (CNSS) was also prepared through an operational audit.

Executive Board Assessment

Executive Directors commended the Guinean authorities for their continued efforts to advance the economic reforms that were launched in the latter part of 1996 and supported by the Fund under a new three-year ESAF arrangement. Through these efforts Guinea has begun to establish a record of policy implementation that is attracting greater investor interest and increased donor support. However, Directors stressed that steadfast implementation of sound financial policies and structural reforms to strengthen the social, physical, financial, and judicial infrastructure was vital to facilitate productive activity in the private sector, and hence more rapid economic growth.

Directors urged continued efforts to keep fiscal consolidation on a firm footing. They welcomed the recent measures to close remaining loopholes in the application of the value-added tax and customs duties to mining companies, and to improve the verification of compliance. However, they underscored that revenue shortfalls are a matter of concern, and that strengthening the mobilization of non-mining revenue remains at the core of Guinea's budgetary program. Thus, Directors cautioned the authorities against deviating from the path set for government revenue in the program. Noting the authorities' reliance in 1997 on a centralized system of cash management, they urged a return to proper budgetary procedures without delay.

Directors commended the Guinean authorities for taking concrete actions aimed at reducing corruption and fraud, including through the tightening of customs administration and reform of the judicial system. Noting that progress in governance is pivotal to the success of financial and

structural adjustment policies, Directors stressed the need to build on improvements in this area and to establish greater transparency in public resource management.

Directors considered that monetary policy in 1997 had been insufficiently tight, and stressed the need to rein in the recent increase in inflation. They urged the authorities to adhere strictly to the monetary program and to reinforce the effectiveness of monetary policy through a more efficient use of indirect instruments, together with a strict limitation of credit to the government.

Directors welcomed the recent removal of a central bank levy on banks' foreign exchange transactions as an important step toward leveling the playing field between the formal and informal markets for foreign currency. They urged the central bank to limit its interventions to the smoothing of short-term fluctuations in the exchange rate and to the achievement of the target for net foreign assets, but to refrain from targeting a specific level of the rate. Directors agreed that the authorities should continue their efforts to address Guinea's external debt problem and negotiate debt relief with all bilateral creditors.

Regarding structural reforms, Directors welcomed the authorities' recent actions to address weaknesses in the financial system, including the closing of one bank and the ongoing restructuring of three others. They strongly supported the authorities' decision to make limited financial support from the government contingent on clear commitments of the key shareholders to the survival of the respective banks in terms of both financial and managerial resources. Directors encouraged the authorities to pursue the reforms of financial institutions, strengthen prudential control, and improve the health of the banking system. They also urged the authorities to proceed with the needed pension reform.

Directors emphasized that improving the quality and timeliness of economic statistics was essential for monitoring economic developments. Directors welcomed the authorities' decision to publish the letter of intent and the policy framework paper, as this would help to achieve broader support for the government's program and enhance the transparency of economic policies.

Press Information Notices (PINs) are a new series of IMF press notices (see Press Release 97/21). PINs are issued, at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

Guinea: Selected Economic Indicators

	1995	1996	1997	1998 Prog.
	Annual percentage change			
Domestic economy				
Changes in real GDP	4.4	4.6	4.7	5.0
Changes in consumer prices (period average)	5.6	3.0	1.9	4.0
	In millions of US$ 1/			
External economy				
Exports, f.o.b.	747.5	695.8	769.8	843.0
Imports, c.i.f.	809.2	713.8	763.1	821.8
Current account balance, excluding official transfers	-332.4	-304.8	-300.7	-302.3
(in percent of GDP)	-8.9	-7.8	-7.7	-7.7
Capital account balance	138.6	99.2	176.2	110.4
Gross official reserves	197.5	169.5	225.4	274.8
(in months of imports)	2.6	2.4	3.0	3.4
Debt service (including to the Fund) 2/	18.7	17.9	16.5	16.6
Change in real effective exchange rate (in percent) 3/	-5.7	2.3	-0.6	...
	In percent of GDP 1/			
Financial variables				
Government revenue	11.0	10.1	11.1	11.6
Domestic primary balance 4/	1.9	1.3	2.8	2.9
Change in broad money (in percent)	11.3	5.8	17.3	9.0
Interest rate 5/	13.0	9.0	9.0	...

Sources: Data provided by the Guinean authorities; and IMF staff estimates and projections.

1/ Unless otherwise noted.
2/ In percent of exports of goods and nonfactor services.
3/ (+) = appreciation.
4/ Excluding external aid.
5/ Minimum annual rate on bank savings deposits.

Press Information Notice (PIN) No. 98/20
FOR IMMEDIATE RELEASE
March 26, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Guinea-Bissau

The IMF Executive Board on March 6, 1998 concluded the 1997 Article IV consultation[1] with Guinea-Bissau.

Background

Guinea-Bissau's adjustment effort was initiated with two programs supported by the annual arrangements under the Structural Adjustment Facility (SAF) in 1987-89. Following a period of mixed economic performance, a period of financial stabilization in 1993-94 led to an economic and financial program supported by a three-year arrangement under the Enhanced Structural Adjustment Facility (ESAF), which was approved by the Executive Board in January 1995. The macroeconomic and structural policies pursued by Guinea-Bissau in the period 1995-97 led to substantial improvement in a number of areas: growth was strong, inflation fell, and internal and external imbalances were reduced.

GDP growth reached 4.5 percent on average in 1995-96, and is estimated to have risen to 5 percent in 1997, spurred by a strong increase in the production of cashew nuts, the principal export crop, and a pickup in investment. However, uncertainties regarding the possible entrance of the country in the Western African Monetary Union (WAMU) and adoption of its currency, the CFA franc, unleashed in midyear market pressures on the national currency, the Guinea-Bissau peso. The resulting sharp depreciation of the peso fed through the domestic prices, increasing inflation. The exchange rate stabilized in the last quarter of 1996, following a tightening of monetary policy and clarifications about the modalities of entrance into the WAMU; as a result, the rate of inflation

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

declined to about 1 percent per month in the last quarter of the year. Over the whole year, the rate of inflation was 66 percent. Inflation fell sharply in 1997 to 16 percent on an end-year basis, with the price level declining in the last four months of the year.

Guinea-Bissau joined the WAEMU, effective May 2, 1997, with its currency exchanged at PG 65 per CFA franc, close to the one prevailing in the month of December 1996. The currency conversion was carried out in the three-month period May-July 1997. The Central Bank of Guinea-Bissau was incorporated in the Central Bank of Western African States (BCEAO) after a recapitalization operation carried out by the government with the financial assistance of foreign donors and creditors. To support the entrance into the monetary union, policies were rigorously pursued to strengthen public finances, involving a tightening of expenditure and improved revenue collection. As a result of these efforts, the revenue/GDP ratio reached 15.4 percent of GDP in 1997, up from 12.5 percent in 1996, and the current primary surplus reached 5.5 percent, compared with 3.3 percent in 1997. A comprehensive tax reform was adopted in October 1997, involving the introduction of a generalized sales tax, the streamlining of the customs tariff, and the reform of excise taxes, including on petroleum prices. These reforms entered into effect in early 1998. The government has also embarked on a major reform of the civil service to improve pay incentives, while increasing efficiency. The expansion of credit was moderate, and the increase of money supply, in the context of a return of confidence, was mainly accounted for by the rise in net foreign assets of the banking system.

The balance of payments improved in 1997, with the external current account deficit declining to 14.2 percent of GDP, from 20.6 percent, as exports of cashew nuts reached a record level, being boosted also by the sale of the large unsold stock accumulated in 1996.

Prospects for 1998

Real GDP is projected at 5.5 percent in 1998, as the output of cashew nuts is expected to increase further, and public investment to strengthen. Inflation is expected to remain subdued, with end-year inflation declining to about 7 percent.

The external current account deficit (excluding official transfers) is expected to deteriorate somewhat, to 18 percent of GDP, as exports would decline relative to 1997, when they were boosted by the sale of stocks.

The current primary fiscal surplus is projected to attain 5 percent of GDP; tax revenue is to be boosted by the newly adopted tax reforms. On the expenditure side, the domestic contribution to investment will increase somewhat, to strengthen the education and health sectors, while current expenditure will be contained.

Executive Board Assessment

The budgetary revenue and primary surplus targets for 1997 had been exceeded owing to stronger-than-expected performance of non-tax revenue, a vigorous tax collection effort toward the end of the year, and expenditure containment. Economic growth continued to be robust, and

inflation had fallen sharply throughout the year, reflecting the regained confidence resulting from the entry of Guinea-Bissau into the West African Monetary Union (WAMU) and the West African Economic and Monetary Union (WAEMU). Directors noted that the return to monetary stability had also led to an improvement in the investment climate, which had facilitated the privatization process. Progress had also been made in other areas of structural reform.

Nevertheless, Directors noted that Guinea-Bissau still faces a number of challenges, with the economy remaining vulnerable to external shocks, a high external debt burden, and widespread poverty. Therefore, to consolidate the recent progress and put the economy on a path of strong and sustainable growth, Directors urged the authorities to strengthen the public finances and deepen structural reforms.

Directors welcomed the comprehensive tax reform that is being implemented, including the introduction of a generalized sales tax due to come into effect on April 1, 1998, and of a new streamlined customs tariff, which would contribute greatly to modernizing the tax system and further improving the fiscal position. They stressed the importance of thorough and timely implementation of these reforms, and of the continued efforts to improve tax and customs administration. They also noted that expenditure management should be further strengthened, including through the elimination of domestic arrears.

Directors welcomed the steps taken by the authorities to start reforming the civil service in depth, and reducing its size while revamping the salary and incentive structure. These reforms should be carried out with determination and without delays, so as to contribute to the improvement of public services, and in particular to allow a strengthening of resources for the social sectors and infrastructure.

Directors noted that significant progress had been achieved in the privatization process. They called on the authorities to continue and broaden the privatization process, and considered that it was important that the private management of other public services—such as the post and telecommunications—be subject to competitive conditions in order to increase efficiency.

Directors welcomed the strengthening of the banking system that was under way, and especially the recapitalization of the largest commercial bank, and noted the importance of intensifying the efforts in this area. They expressed the view that, with the restoration of price stability, a favorable environment had now been established to broaden the financial system, and in particular to develop savings and loan institutions geared to the financing of small-scale enterprises.

Directors noted that debt management remains weak, and welcomed the steps taken recently to establish a national debt monitoring committee and install a computerized debt management system. They urged the authorities to regularize speedily their relations with all creditors, including Paris Club, non-Paris Club, and a number of regional multilateral creditors.

Directors noted Guinea-Bissau's very heavy external debt burden, and emphasized that a strong and sustained track record in policy implementation was needed before reaching a decision point under the HIPC debt initiative.

Press Information Notices (PINs) are issued, at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

Guinea-Bissau: Selected Economic Indicators 1/

	1994	1995	1996	1997	1998 Prog.
	(Annual percentage change)				
Change in real GDP	3.2	4.4	4.6	5.1	5.5
GDP deflator	23.3	44.7	49.8	39.5	10.2
Change in consumer prices (end of period)	19.3	49.7	65.6	16.8	7.0
	(In percent of GDP)				
Gross domestic investment	21.8	22.3	23.0	19.1	22.3
Gross domestic savings	3.9	-1.2	1.8	3.3	2.5
Gross national savings	11.5	6.2	8.3	14.0	11.5
	(In millions of U.S. dollars) 2/				
Export, f.o.b.	20.5	23.9	21.6	53.9	42.4
Imports, f.o.b.	-53.8	-59.3	-56.8	-67.9	-73.7
Current account balance, excluding official transfers	-48.6	-59.9	-55.8	-37.7	-57.2
Capital account balance	-10.2	24.1	20.0	22.5	11.5
Gross official reserves	18.4	20.3	11.8	31.2	...
Current account balance, excluding official transfers (in percent of GDP)	-16.2	-23.6	-20.6	-14.2	-18.5
Change in real effective exchange rate (in percent) 3/	-11.0	-7.6	4.8	12.4	...
External public debt (in percent of GDP)	376.5	367.1	339.1	356.4	...
	(In percent of GDP) 2/				
Financial variables					
Government revenue	12.4	12.7	12.5	15.4	14 7
Government expenditure and net lending 4/	35.5	30.4	33.6	37.5	29.3
Current primary fiscal balance	3.3	4.0	3.3	5.5	5.0
Overall government balance 5/	-4.6	-17.7	-18.0	-12.6	-14.6
Change in broad money (in percent)	33.9	25.9	33.2	53.5	15.0
Interest rate (in percent) 6/	26.0	39.0	54.0	6.2	...

1/ IMF staff estimates.
2/ Unless otherwise noted.
3/ (+)=appreciation.
4/ Includes in 1997 the cost of the recapitalization of the Central Bank.
5/ Excluding grants and restructuring operations.
6/ Central Bank rediscount rate.

Press Information Notice (PIN) No. 98/5
FOR IMMEDIATE RELEASE
February 16, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Article IV Consultation Discussions held in 1997 with the People's Republic of China in Respect of the Hong Kong Special Administrative Region

The IMF Executive Board on January 26, 1998 considered a report on the Article IV consultation[1] discussions with People's Republic of China—Hong Kong Special Administrative Region, which were held in late 1997.

Background

The return of Hong Kong to the People's Republic of China took place on July 1, 1997. The terms of the transfer, which are embodied in the Basic Law, included the establishment of the Hong Kong Special Administrative Region (SAR). The Basic Law also provides the SAR a considerable degree of autonomy over economic and other policies, and includes a commitment to the continuation of the existing free-market system for 50 years.

The Basic Law's requirements in the area of fiscal policy include the avoidance of fiscal deficits and the principle of keeping the budget commensurate with the growth rate of GDP. In FY 1997, a surge in land-related revenues is expected to cause the fiscal surplus to exceed the budget target of 2¼ percent of GDP by a substantial margin. As a result, fiscal reserves (including the balance of the Land Fund) are expected to rise to over 30 percent of GDP.

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the economy, collects economic and financial information, and discusses with officials economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the authorities. In this PIN, the main features of the Board's discussion are described. As a Special Administrative Region of the People's Republic of China, Hong Kong SAR is not a member of the IMF. However, annual consultation discussions have been held with the Hong Kong SAR authorities since October 1990.

The Basic Law also requires that Hong Kong SAR's currency be fully backed by foreign reserves, and the exchange rate is linked to the U.S. dollar under a currency board-type arrangement. As of end–December 1997, foreign currency assets totaled US$92.8 billion.

Real sector developments were generally favorable in 1996 and the first half of 1997, but activity showed signs of slowing during the latter half of 1997, owing to the impact of the regional crisis. Real GDP growth accelerated to 5 percent in 1996, following below-trend growth of 3.9 percent in 1995, reflecting strength in private investment and consumption, as well as the impact of a significant narrowing of the deficit in goods and nonfactor services trade. During the first half of 1997, GDP growth reached 6.4 percent, owing to strength in domestic demand that offset a widening of the trade deficit. Growth is expected to have slowed in the second half of 1997—for an average of 5¼ percent for the year as a whole—as a result of the effect of the regional crisis on external trade, as well as the impact on domestic demand of higher interest rates and declines in stock and property prices.

As a result of the pickup in activity to mid–1997, the economic slack that emerged in 1994–95 appeared to have been virtually eliminated. Output at mid–1997 is estimated to have exceeded potential and the unemployment rate dipped to 2.2 percent in the third quarter of 1997, compared with 2.6 percent a year earlier. Reflecting labor market tightness, real wage growth accelerated to 1.7 percent during the four quarters ending in September 1997. However, price pressures were contained—composite CPI inflation was 5.2 percent in December, down from 6.4 percent in July.

The regional crisis contributed to substantial financial market volatility. Stock and property prices rose strongly during the first half of 1997—by mid-1997, property prices were a third higher than their trough in the second quarter of 1994, and the Hang Seng stock price index reached an historical peak in early August, having risen by around 50 percent during the previous 12 months.

However, spillovers from the regional turmoil caused the Hong Kong dollar to come under speculative pressure in the latter half of 1997. Pressures on the exchange rate were successfully resisted by means of intervention in the foreign exchange market and a corresponding tightening of domestic liquidity. Nonetheless, higher interest rates, which resulted from spillovers from the financial turmoil in the region and the resultant pressures on the exchange rate, as well as weaker sentiment contributed to a substantial correction in stock and property markets. By end–January 1998, the Hang Seng index was roughly 45 percent below its 1997 peak, and property prices appear to have fallen by 15–20 percent on average since mid–1997. Although spreads between rates on short-term Hong Kong dollar deposits and U.S. dollar deposits have narrowed, they remain well above the historical average, and major Hong Kong SAR banks responded by hiking their prime interest rate in early January 1998 by 75 basis points.

Executive Board Assessment

Executive Directors observed that, notwithstanding the recent turmoil within the region, developments in Hong Kong SAR during the past year had been satisfactory in many respects. The handover had been achieved smoothly, and confidence in a continuation of the existing economic and legal framework had been maintained under the "one country, two systems" framework. In addition, the economy continued to recover during 1997 from the slowdown of 1994–95, consumer inflation had been contained, the fiscal position strengthened markedly, and foreign exchange reserves increased significantly. Directors observed that, more recently,

Hong Kong SAR's solid fundamentals and decisive policy actions had helped it withstand the regional financial crisis and the bouts of speculative attack. In particular, they welcomed that the Hong Kong SAR Government (SARG) had allowed a prompt tightening of domestic monetary conditions under the linked exchange rate system to counter the pressures in the foreign exchange market.

Nonetheless, Directors agreed that the regional crisis significantly clouds the short-term prospects for Hong Kong SAR and exposes it to some vulnerability. In these circumstances, Directors stressed the importance of preserving confidence in the SARG's commitment to a rules-based and noninterventionist policy framework, and ensuring that policies remain supportive of the economy's historical flexibility. They also emphasized the need to maintain strong regulatory oversight over the financial system, especially given the burden on the banking sector of high interest rates and the decline in real estate prices. These policies would help limit the impact of the regional crisis and, as in the past, provide the foundation for Hong Kong SAR's continued economic success in the period ahead.

Directors endorsed the Hong Kong SARG's commitment to the linked exchange rate system, which was demonstrated by its firm adherence to the link in the face of recent speculative attacks. They agreed that the system had provided an important anchor for economic stability since 1983, and that it currently plays a vital role in demonstrating the commitment to an independent monetary and exchange rate policy in Hong Kong SAR, and in maintaining confidence in its status as an international financial center. They emphasized the importance for the exchange rate link of maintaining substantial foreign exchange reserves, a fiscal surplus, and flexible factor markets. While the costs associated with maintaining a linked exchange rate system were recognized, Directors agreed that these were outweighed by the benefits, in Hong Kong SAR's case. In this connection, Directors also welcomed the Chinese authorities' commitment not to devalue the Renminbi, which should further enhance confidence in the maintenance of Hong Kong SAR's linked exchange rate system.

Directors expressed confidence that the economy of Hong Kong SAR would respond flexibly to the impact of the regional crisis, as it had responded to adverse shocks in the past. However, they noted that the openness and liquidity of its financial markets meant that Hong Kong SAR remains vulnerable to shifts in investor sentiment. In these circumstances, and given the continued regional turmoil, Directors suggested that monetary conditions should remain tight in order to maintain confidence in the Hong Kong SARG's commitment to the exchange rate link.

Directors expected that higher interest rates and the effects of the regional crisis on trade would contribute to a noticeable slowdown in activity in Hong Kong SAR during 1998. Indeed, the continued uncertainties about the magnitude and duration of the regional slow down mean that a further reduction in growth cannot be discounted. The outlook for Hong Kong SAR also depends importantly on developments on the mainland of China, given the important linkages between the two economies, and growth on the mainland is expected to slow down somewhat in 1998. Nevertheless, the expected easing of demand was seen as desirable, in view of the signs of overheating that emerged during the past year, including asset price inflation, rapid credit growth, and labor market tightness. A reduction of these pressures would have the welcome effect of facilitating an improvement in Hong Kong SAR's competitiveness, which was adversely affected by currency depreciations within the region. While noting that the recent corrections in asset prices are already contributing in this regard, Directors stressed the importance of continued flexibility in goods and factor markets, especially with regard to wage developments. In this

regard, a few Directors noted that the scope for further sharp gains in productivity may be more limited in the future.

Directors commended the Hong Kong SARG for the firm prudential and regulatory oversight of the financial sector and for the recent improvement in disclosure requirements. This commitment, and the strong capital position and profitability of the domestically incorporated banks, helped provide confidence that the system would weather the impact of the regional crisis. Nonetheless, Directors suggested that a further broadening of disclosure requirements could help reduce market uncertainty and limit the risk of unwarranted contagion. In this regard, they welcomed the Hong Kong SARG's willingness to allow weaker financial institutions to fail, in line with its overall noninterventionist approach to policies. They stressed the need to ensure that banks adhere more closely to existing guidelines on property lending, in order to reduce the financial sector's exposure to the real estate sector. Directors welcomed the intention to develop a market for mortgage-backed securities, which would enable banks to improve their liquidity and risk management. A few Directors questioned whether it is appropriate to set up a government-owned mortgage corporation, but noted the Hong Kong SARG's intention to eventually privatize the mortgage corporation. They stressed the importance of ensuring that the mortgage corporation's activities did not transfer risks related to mortgage lending to the public sector.

Directors endorsed the Hong Kong SARG's continued commitment to prudent fiscal policies under the Basic Law. They considered that maintaining a surplus during the coming fiscal year would help moderate aggregate demand pressures, and they urged the authorities to avoid including measures in the 1998 budget that would ease the underlying fiscal stance. Moreover, Directors noted that, particularly at this juncture, large fiscal reserves play an important role in signaling the authorities' continued commitment to the rules-based policy framework. Directors agreed that fiscal reserves also provide reassurance that resources would be available to cope with the longer-run pressures that will result from an aging population.

Directors endorsed the Hong Kong SARG's effort to rationalize housing policies, and encouraged efforts to reduce public sector intervention in the housing market. Directors also welcomed the Hong Kong SARG's continued commitment to a noninterventionist industrial policy framework. In their view, programs aimed at promoting specific industries or sectors risked impairing the flexibility of goods and labor markets. Indeed, they encouraged measures to improve the competitive environment within the nontraded services sector, including through further deregulation, as a means of reducing business costs.

Directors commended the Hong Kong SARG for its efforts to improve the timeliness and accuracy of economic data for Hong Kong SAR. However, they called for further early progress, particularly with regard to the timeliness of data on foreign reserves and the timeliness and availability of data on the capital account of the balance of payments, as well as data on short-term liabilities and banking and corporate sector data. Such improvements would help in monitoring Hong Kong SAR's external position.

Press Information Notices (PINs) are a new series of IMF press notices (see Press Release 97/21). PINs are issued, at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

People's Republic of China, Hong Kong Special Administrative Region: Selected Economic and Financial Indicators

	1994	1995	1996	1997
Real GDP (percent change)	5.4	3.9	5.0	5.3 **1/**
Real domestic demand	11.8	7.1	3.4	8.0 **1/**
Foreign balance (contribution)	-5.9	-3.3	1.4	-2.9 **1/**
Saving-investment balance (percent of GDP)	1.2	-4.3	-1.7	-2.5 **1/**
Gross domestic saving	33.1	30.5	30.7	31.1 **1/**
Gross domestic investment	31.9	34.8	32.3	33.6 **1/**
Inflation (percent change)				
Consumer prices	8.1	8.7	6.0	5.7
GDP deflator	6.9	2.6	5.4	6.5 **1/**
Employment (percent change)	2.6	1.1	3.5	...
Unemployment rate (percent)	1.9	3.2	2.8	...
Real wages	1.3	-1.0	0.4	1.0
Government budget (percent of GDP) **2/**				
Revenue	17.3	16.7	17.5	19.7 **1/**
Expenditure	16.2	17.0	15.3	15.9 **1/**
Consolidated budget balance	1.1	-0.3	2.2	3.8 **1/**
Reserves at March 31 **3/**	14.9	13.7	14.6	32.1 **1/**
Money and credit (percent change, end-period)				
Narrow money (M1)	-1.2	2.8	14.2	-4.3
Broad money (M3)	13.6	14.2	10.5	8.2
Loans for use in Hong Kong SAR	17.0	11.1	17.1	24.7
Interest rates (percent, end-period)				
Best lending rate	8.5	8.8	8.5	9.5
Three-month HIBOR	6.3	5.9	5.5	9.1
Merchandise trade (percent change)				
Export volume	10.4	12.0	4.8	5.0 **1/**
Domestic exports	-2.3	1.9	-8.4	2.0 **1/**
Reexports	13.8	14.3	7.5	5.6 **1/**
Import volume	14.0	13.7	4.3	6.3 **1/**
Export value	11.9	14.9	4.0	4.2
Import value	16.7	19.2	3.0	5.2
External balance (in billions of US$)				
Merchandise trade balance	-10.9	-19.6	-18.4	-20.5 **1/**
In percent of GDP	-8.4	-14.1	-11.9	-11.8 **1/**
Goods and nonfactor services balance	1.6	-6.0	-2.6	-4.3 **1/**
In percent of GDP	1.2	-4.3	-1.7	-2.5 **1/**
Foreign exchange reserves (in billions of U.S. dollars, end of period)	49.3	55.4	63.8	92.8
(In months of retained imports)	9.9	9.1	10.9	15.0

Sources: Data provided by the Hong Kong SAR authorities; and staff estimates and projections.
1/ Staff estimates.
2/ Fiscal year begins April 1.
3/ Fiscal reserves at end-FY 1997 include the projected HK$205 billion balance in the Land Fund (15.3 percent of GDP).

Press Information Notice (PIN) No. 98/16
FOR IMMEDIATE RELEASE
March 10, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Israel

The IMF Executive Board on February 11, 1998 concluded the 1997 Article IV consultation[1] with Israel.

Background

After several years of strong economic performance, the Israeli economy experienced a bout of fiscally induced overheating in 1995–96. A sharp tightening of monetary policy was needed in the absence of fiscal correction to deal with these excess demand conditions but had an inevitable impact on the economy. The situation was further exacerbated by extraneous events such as a deteriorating security situation and an unwinding of the effects of the early-1990s' immigration wave. As a result, growth in 1997 was disappointing (2 percent), as was the concomitant sharp rise in unemployment (to almost 8 percent).

On the positive side, sluggish domestic demand and quiescent wage pressures against the background of the tight monetary policy led to a marked reduction in inflation during 1997, with the 12-month change in the overall CPI brought down to 7 percent by the end of the year, at the bottom of the authorities' target range. Weakening demand in Israel and strengthening demand abroad, in combination with an improvement in the terms of trade caused by the appreciation of the U.S. dollar against European currencies, led the external current account deficit—which had ballooned from near balance early this decade to 5½ percent of GDP in 1996—to narrow to about 3½ percent of GDP in 1997.

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

Fiscal policy was tightened significantly in 1997. Having missed their fiscal targets for 1995 and 1996, the authorities strengthened their commitment to deficit reduction in 1997 with exceptionally strong efforts to rein in expenditures during the year. While final information for the year is not yet available—the target was an overall deficit of 2.8 percent of GDP—the 1997 outturn is likely to have represented a very significant improvement over that in 1996, especially in structural terms given the weak pace of economic activity. However, the level of the public-debt-to-GDP ratio, which stood at 103 percent in June 1997, is still very high. In early January 1998, the Knesset approved the state budget for 1998, targeting a deficit of 2.4 percent of GDP based on restraining the growth of expenditures.

Monetary policy in Israel aims at achieving an inflation target set by the government while simultaneously maintaining a commitment to keep the shekel trading within its diagonal exchange rate band. Over much of the past year, the shekel was kept at or near the appreciated limit of the diagonal exchange rate band as capital inflows exceeded those needed to cover the current account deficit. In order to maintain the exchange rate within the band, the Bank of Israel had to engage in foreign exchange intervention and subsequent sterilization, greatly increasing the share of net foreign assets in the money base. In June, the authorities approved a widening of the band from 14 percent to 28 percent by adjusting the limit on depreciation. Subsequent to the widening of the band, there was a steep drop off in capital inflows and, as a result, the Bank of Israel did not need to further intervene in the foreign exchange market.

Structural reform is an important element of the government's economic program aimed at sustained growth. During 1997, significant progress was made in the areas of privatization—especially in regard to the banks—and the liberalization of capital account transactions.

In 1998, growth is projected to rebound somewhat under the assumption that the policy mix will shift in the direction of a better balance between fiscal and monetary policies and that the negative effects on growth of the security situation will ease.

Executive Board Assessment

Directors observed that, while growth had slowed and unemployment had risen in 1997, there were a number of encouraging features in economic developments that augured well for future economic performance. Of particular importance was the authorities' success in attaining their targets for the fiscal deficit and inflation, as well as the substantial progress in structural reforms. Nevertheless, with unemployment rising, the economic situation remains difficult, and Directors called for vigorous efforts to set conditions that would permit sustained growth in line with Israel's potential, together with a further substantial drop in inflation and a viable external position. They advocated steady pursuit of a strategy of strong and sustained fiscal consolidation and bold structural reform that would reduce the burden on monetary policy. Directors also stressed the critical role of the peace process for economic prosperity in Israel and the region.

Directors welcomed the achievement of the 1997 fiscal deficit target, which signaled a turnaround in the conduct of fiscal policy from the previous two years, when the deficit targets had been exceeded. Looking ahead, they stressed the importance of building on this achievement by launching an ambitious medium-term fiscal consolidation plan that would bring

the deficit down to the low levels now being targeted in other advanced countries and reduce Israel's still high public-debt-to-GDP ratio, while helping to prepare for the looming problems in the health and pension systems. Directors considered that the current medium-term plan, albeit in the right direction, is not sufficiently strong. They urged the authorities to press ahead with stronger adjustment aimed at achieving, at least, approximate balance by 2001 (in terms of the government's accounting system). They noted that budgetary retrenchment along these lines would facilitate the task of monetary policy in lowering inflation, with consequent beneficial effects on the real interest rate and the real exchange rate, both of which are crucial to Israel's growth. Directors also noted that Israel's use of a fiscal accounting system akin to an operational budget concept obscured international comparisons of the fiscal situation, and that Israel's budget deficit remains high by conventional standards of measurement.

In view of the need for a more ambitious medium-term fiscal consolidation effort than currently envisaged, Directors regarded the fiscal adjustment planned for 1998 as the minimum required, and stressed the critical importance of actually achieving the target, including through recourse to supplementary packages and contingencies in the budget if revenues turn out weaker than expected. Given the large size of the public sector in Israel, Directors strongly endorsed the emphasis in the 1998 budget on expenditure containment, in particular the curbing of the public sector wage bill.

Turning to monetary policy, Directors commended the authorities for persevering with a tough stance during 1997, which had resulted in inflation coming in at the bottom end of the target range. They encouraged the authorities to seize the opportunity provided by current favorable conditions to lower inflation further in 1998, to consolidate the progress made last year, and to make a major inroad into Israel's long-held inflation psychology. To this end, Directors saw the need for lowering the inflation target range for 1998. They were confident that, with support from the full implementation of the 1998 budget, continued visible progress with disinflation would be compatible with, and would facilitate, a gradual but cumulatively meaningful easing of monetary conditions.

As regards the operational framework of monetary policy, Directors welcomed the increasingly forward-looking approach to inflation targeting being adopted by the Bank of Israel, and encouraged the authorities to extend the operational horizon for setting inflation targets. They noted that the credibility and transparency of this approach would be enhanced by the announcement of a clear and specific target path for medium-term disinflation to the level of other advanced countries. Moreover, most Directors were of the view that the achievement of this target path for inflation should be given primacy over the exchange rate, with the proviso that the task of keeping the real exchange rate within a viable range should be handled appropriately by fiscal and structural policies. To strengthen public accountability, Directors urged the Bank of Israel to publish regularly a report on the inflation outlook and the policies needed to keep inflation on track. Commenting on the ongoing debate on the central bank law, Directors observed that international experience underscores the importance of preserving the operational independence of the central bank, whose primary responsibility should be to achieve and maintain price stability. Any changes to the law governing the Bank of Israel should be drafted in accordance with this basic principle.

In the area of structural policies, Directors welcomed the concrete actions taken in 1997 to reduce the role of the state in the economy and to promote competition. Particularly notable was the successful acceleration of privatization—especially of banks—and Directors urged the authorities to seek to maintain this momentum in 1998 and beyond. Despite the significant achievement in 1997, Directors observed that more work needs to be done in a number of structural areas to set the stage for strong and sustained growth over the medium term. They identified in this connection domestic capital market reform, additional measures to increase competition, deindexation, and reform of the minimum wage system.

Directors commended the authorities for the steps they had taken over the past year to further liberalize capital account transactions. It was noted that the recent widening of the exchange rate band was consistent with these developments. While strongly supporting the authorities' efforts in liberalizing the capital account, Directors stressed that this increased the importance of close supervision of the banking system and close monitoring of short-term external borrowing, as well as the maintenance of sound macroeconomic policies.

Press Information Notices (PINs) are issued, at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

Israel: Selected Economic Indicators

	1993	1994	1995	1996	1997 1/
	(Percentage change, unless otherwise indicated)				
National accounts (constant prices)					
Real GDP	3.4	6.8	7.1	4.5	2.0
Private consumption	7.3	9.2	7.4	5.2	3.8
Public consumption	4.6	0.1	1.8	5.5	2.0
Gross capital formation	4.3	8.6	10.2	6.8	-6.7
Exports of goods and services	10.5	12.6	10.1	5.0	8.6
Imports of goods and services	14.2	10.9	8.6	7.6	4.0
Labor market indicators					
Israeli civilian labor force	4.8	4.3	3.5	2.2	2.3
Overall employment	6.1	6.8	5.2	2.5	1.2
Unemployment rate (in percent)	10.0	7.8	6.9	6.7	7.7
Prices (end period)					
Overall CPI	11.3	14.4	8.1	10.6	7.0
Underlying CPI (excluding housing, fruits and vegetables)	8.1	9.7	8.8	10.1	6.7
Money and credit (period average)					
Narrow money (M1)	23.7	20.6	8.4	14.9	14.3
Broad money (M3)	24.9	26.2	25.5	26.5	24.7
Nondirected credit	44.9	28.1	26.2	21.6	18.5
Interest rates (average, in percent)					
Discount-window loan	11.3	13.4	15.5	16.1	14.3
Nondirected credit in new sheqalim	16.5	17.4	20.2	20.7	18.7
Public finance (percent of GDP)					
Central government balance	-2.5	-2.4	-4.2	-3.8	-2.8
General government balance	-3.5	-2.2	-3.4	-4.1	...
Public debt (at June)	115.0	109.0	103.0	101.0	103.0
Balance of payments					
Trade balance (percent of GDP)	-8.8	-7.5	-8.7	-8.0	-5.4
Current account (percent of GDP)	-2.7	-3.4	-5.6	-5.6	-3.5
Foreign reserves (average, in US$ millions)	5,711	6,274	8,637	9,939	17,165
Exchange rate and terms of trade indices					
Nominal effective exchange rate (1990=100)	-8.2	-7.6	-6.1	-2.7	0.2
Real effective exchange rate (1990=100)	-1.2	1.1	0.8	5.9	7.3
Terms of trade (1990=100; index level)	110.5	106.7	100.5	101.0	...

Sources: Data provided by the Israeli authorities; and IMF, International Financial Statistics.

1/ Staff preliminary estimates.

Press Information Notice (PIN) No. 98/4
FOR IMMEDIATE RELEASE
February 3, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Kuwait

The IMF Executive Board on October 15, 1997 concluded the 1997 Article IV consultation[1] with Kuwait.

Background

Following the successful completion of reconstruction and the restoration of oil output in the years immediately following the 1990–91 regional crisis, the focus of Kuwait's economic policies has been on eliminating financial imbalances, addressing the difficulties in the financial system, and creating the appropriate environment for private sector growth. Significant progress has been made toward these goals. The fiscal deficit was reduced substantially to 4 percent of GDP in 1995/96, from 10 percent the previous year and 18 percent in 1993/94. In 1995, for the first time since the Gulf war, the balance of payments recorded an overall surplus equivalent to 15 percent of GDP. Progress was also made in resolving the difficult bank debt problem through the implementation of the Debt Collection Program (DCP).

Economic and financial conditions continued to improve sharply in 1996 reflecting higher international oil prices, and the pursuit of appropriate financial policies. While crude oil output remained practically unchanged from the 1995 level, in line with Kuwait's OPEC quota, export prices rose from an average of US$15.57 per barrel to US$18.34. Activity in the non-oil sectors is estimated to have risen by some 2 percent in real terms, with growth

[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

mainly driven by construction in the petrochemical sector and sustained activity in the financial and other services. Thus, while total real GDP rose by 0.9 percent, real income—adjusted for the terms of trade effects—increased by about 12 percent. Inflation remained low, at about 2 percent.

The fiscal position is estimated to have improved markedly, registering a surplus of 9 percent of GDP in 1996/97, enabling the authorities to return to their policy of building assets for future generations. The balance of payments also benefited from higher oil export prices, which generated an increase in export receipts of 17 percent. Imports grew by about 7 percent and the net service deficit declined because of higher investment income, leading to a rise in the external current account surplus to the equivalent of 23 percent of GDP, from 17 percent in 1995. In 1996, Kuwait repaid the last installment of the 1992 syndicated loan of US$5.5 billion and the overall balance of payments was also in surplus (US$2.6 billion), strengthened by increases in exports and private capital inflows.

The domestic debt problem—which developed as a result of collapses of the informal stock exchange in 1982 and from the loss of assets following the Gulf war—continued to be addressed appropriately, and bank supervision and prudential regulations were enhanced. The improved confidence was buoyed by the continued successful divestiture of government shares in commercial enterprises.

Preliminary estimates for 1997 point to a slightly less favorable financial performance than in 1996 as a result of adverse terms of trade developments. Crude oil output is expected to remain unchanged, but export prices are projected to decline by some US$1 per barrel, thus resulting in an estimated fall in nominal oil GDP of about 5 percent. However, owing to increased refining capacity and petrochemical production, together with higher capital expenditure under the 1997/98 budget, total real GDP could grow by about 1 percent. The fiscal position, including investment income, is likely to remain in surplus, taking into account current oil price projections. Similarly, the external current account is projected to record a surplus of about 25 percent of GDP and the overall balance will also be in surplus.

Executive Board Assessment

Executive Directors commended the authorities for the significant progress achieved in 1996 in eliminating fiscal imbalances, enhancing bank supervision, making progress toward resolving the difficult debt problem, and moving forward with the divestiture program. Reflecting that progress, and aided by higher oil export prices, confidence had improved, economic activity had picked up, inflation had remained low, and the stock of foreign assets had risen.

Directors noted that those favorable developments offered a sound basis for an ambitious medium-term program of structural reforms aimed at diversifying the economic base, strengthening the role of the private sector in economic activity, and providing employment opportunities for the growing number of Kuwaitis entering the labor force.
Directors observed that commendable progress had been made in the sale of government shares in commercial enterprises, and they urged the authorities to proceed with the next phase

of privatization, involving the transfer to the private sector of public utilities and services. Prompt approval of the legislation currently before the National Assembly—the Five-Year Plan and the Privatization Bill—would be important to lay the foundation for the privatization program, as well as other key elements of the medium-term structural reform agenda. Directors also emphasized the importance of permitting greater private sector participation, local and foreign, in all sectors of the economy. Directors stressed the need to pursue labor market reform, in particular to preserve labor market flexibility. Directors generally cautioned against the setting of quantitative requirements governing employment of Kuwaiti nationals in the private sector. Instead, they thought that the emphasis should be placed on education and training, removing disincentives for Kuwaitis to seek employment in the private sector, and fostering the development of the private sector.

Directors noted that, notwithstanding the relatively favorable fiscal prospects over the medium term, the structure of the budget would need to be strengthened by raising the share of non-oil revenues, in order to minimize the volatility of revenues, and by rationalizing spending consistent with the need to transfer responsibilities from the public to the private sector and to enhance resource allocation. Revenue-raising measures could include a restructuring of company taxes, the introduction of a consumption tax, and increases in fees and charges on public sector services. Expenditure measures should aim at reducing subsidies and transfers and at containing the growth of wages and salaries through an overhaul of the salary and benefit structure. Directors welcomed the authorities' intention to pursue continued expenditure restraint, but disappointment was expressed that the additional revenue measures proposed in the 1997/98 budget had not been adopted by the National Assembly, given the contribution of such measures to improving the structure of the budget.

Directors noted that the steps taken to enhance bank supervision, together with the successful implementation of the Debt Collection Program (DCP), had strengthened the soundness of the financial system and reduced moral hazard risks. They stressed, in particular, the need for continued vigilance in enforcing repayments under the DCP. Directors encouraged the authorities to continue to rely on indirect instruments of monetary management, and they welcomed the consideration being given to the possible elimination of the interest rate ceiling.

Directors commended the authorities for pursuing an open exchange and trade system and prudent fiscal and monetary policies in support of the pegged exchange rate arrangement, which had served the economy well.

Directors commended Kuwait for its very generous foreign economic assistance program.

Directors encouraged the authorities to continue in their efforts to make further substantial progress to improve statistics, particularly data on national accounts and prices, and public finances.

Press Information Notices (PINs) are a new series of IMF press notices (see Press Release 97/21). PINs are issued, at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

Kuwait: Selected Economic Indicators, 1994–97

	1994	1995	1996 1/	1997 2/
	Percent change			
Output and prices				
Real GDP	8.4	1.0	0.9	1.3
Real non-oil GDP	5.5	3.3	2.3	2.2
Consumer price index 3/	2.5	2.7	1.8	1.7
	In percent of GDP			
Financial variables *4/*				
Overall fiscal balance (deficit -)	-17.7	-10.3	-4.2	9.1
Total revenue	42.6	47.4	50.2	57.7
Of which: oil revenue	31.8	36.1	36.7	43.8
Investment income	7.8	8.6	10.9	11.2
Total expenditures	60.3	57.7	54.4	48.5
Change in broad money (in percent) 5/	5.4	9.4	-0.6	3.0
Interest rate (in percent) 5/	6.31	7.43	6.98	6.97
	In millions of U.S. dollars			
External sector				
Balance of payments				
Exports	11.1	12.6	14.7	14.3
Of which: oil	10.3	11.9	13.9	13.5
Imports	6.7	7.2	7.7	7.9
Current account	2.5	4.6	6.8	7.3
Overall balance	-3.1	4.0	2.6	2.5
Real effective exchange rate (percent change)	-0.39	-7.84	1.45	1.91

1/ Preliminary data.
2/ IMF staff estimates.
3/ CPI data for 1996 are through November.
4/ Public finance data are for fiscal years ending June 30. GDP on fiscal year basis. projections for 1997.
5/ Monetary data and interest rates are through end-July 1997.

Press Information Notice (PIN) No. 98/30
FOR IMMEDIATE RELEASE
April 14, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Latvia

The IMF Executive Board on March 23, 1998 concluded the Article IV consultation[1] with Latvia.

Background

Latvia has reached an advanced stage of transition and macroeconomic stabilization, and is now in the process of putting in place the comprehensive structural changes required to establish the institutional basis of a market economy. The authorities have established a record of prudent financial policies, enhanced the soundness of the banking system, and moved forward on a broad front of structural reforms.

These policies were reflected in very good economic performance during 1997. Real GDP growth accelerated in the second half of 1997, and is estimated at 6 percent for the year. Reflecting this strong economic growth, official unemployment has begun to decline, falling from 7½ percent in mid-year to 7 percent at end-January 1998. Inflation has declined steadily, reaching 7 percent at end-year, and falling further to just over 6 percent by end-February 1998. Excluding increases in remaining administered prices, such as for utilities and housing, consumer prices rose by just 4.5 percent during 1997. The external current account deficit for 1997 is estimated at just under 7 percent of GDP, while continued strong inflows of foreign direct investment contributed to a balance of payments surplus, and the external public debt-to-GDP ratio declined to about 7 percent of GDP.

A prudent fiscal policy stance has been a major contributor to lower inflation and interest rates

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

and higher private sector investment. The general government accumulated a fiscal surplus of 1.3 percent of GDP in 1997. Revenue increased as a percent of GDP, owing to improvements in tax administration and the impact of increased profits on the corporate income tax. On the expenditure side, smaller-than-expected increases in indexed transfers resulting from the better inflation performance, lower interest payments, and shortfalls in public investment all contributed to the sizable surplus. This trend has continued through the first two months of 1998, with a significant general government surplus accumulated through February; for 1998 as a whole, the general government is expected to show a small fiscal deficit.

Monetary developments during 1997 reflected a continued increase in confidence in economic policies and the banking system, and an acceleration in the development of the financial sector. Broad money grew by nearly 32 percent during the year, in real terms, while velocity declined substantially. Despite rapid growth in domestic credit to the nongovernment sector, equal to 69 percent in real terms for the year, Latvia's domestic credit-to-GDP ratio, at about 10 percent, remains quite low by international standards. Although interest rates on bank deposits are slightly below current inflation, the level of deposits grew by 57 percent last year, reflecting increased confidence in the banking system and strong expectations of further inflation decline. Real interest rates increased during 1997, and have continued this trend thus far in 1998, and virtually all real interest rates are now positive on a forward-looking basis. Banking supervision continued its improvement since the banking crisis of 1995, and the banking system has strengthened considerably. Financial sector regulation is being further enhanced in 1998, including by expanding the focus of financial oversight to the growing number of nonbank financial institutions.

Latvia made significant progress in liberalizing trade in 1997, and the regime is characterized by generally low tariffs (with the exception of some agricultural goods), no quantitative restrictions and virtually automatic import licensing, and only a few specific import tariffs and export duties. Free trade agreements now exist with 25 countries while Most Favored Nation agreements exist with 22 countries. Substantial progress has been made toward accession to the WTO, with agreements on bilateral negotiations effectively reached with all but one country.

Good overall progress has been made on implementing structural reforms. With respect to enterprise privatization, over 300 purchase agreements were concluded in 1997 (about 200 remain) and the private sector now accounts for about 65 percent of GDP. However, the process of privatizing the largest infrastructure enterprises has slowed somewhat, and may not be completed during 1998. Apartment privatization has moved ahead as scheduled, with over 20 percent of all previously government-owned apartments now in private hands, and measures have been taken to speed progress over the medium term. In the area of enhancing property rights, land registration is advancing, and draft legislation before parliament would establish registers for movable property, further supporting credit market development. With regard to the public sector, the process of improving tax administration is continuing, a civil service census was completed and recommendations for public sector reform drafted, and legislation for the second stage of pension reform is being prepared.

Executive Board Assessment

Executive Directors commended the authorities for their prudent financial policies, which had cemented macroeconomic stability, and for making substantial headway toward putting in place the comprehensive structural changes required to establish a market economy.

Directors reviewed progress under the Stand-By Arrangement and noted that continued prudent fiscal and monetary policies, combined with progress on a broad range of structural reforms, had contributed to better than expected results for economic growth and inflation. All performance criteria at end-December 1997 had been met, except for a structural performance criterion. However, Directors noted that Latvia's economy still faces important challenges and risks in both the short term and medium term, stemming from rising pressures for higher spending and a slowdown in the privatization of large enterprises. Therefore, they stressed the importance for the authorities to maintain prudent macroeconomic policies and to accelerate the pace of structural reforms, with a view to creating the conditions for sustained economic growth and full integration into the European economy.

Directors noted that a tight fiscal policy had been a major contributor to Latvia's positive economic performance, but expressed concern that the approved budget for 1998 shows a significantly larger deficit than in the program. They urged the authorities to maintain a tight fiscal stance and to resist the growing election-year pressures for increasing spending. Directors noted the gains made in tax administration, in particular for customs and social taxes, and encouraged the authorities to continue improving tax collection. In this context, Directors expressed a strong concern about expanded use of tax-free economic zones, which tend to complicate tax administration, reduce transparency, and distort economic decision making. They urged the authorities to develop more appropriate policies for regional development. Directors also encouraged the authorities to continue the ongoing pension reform, accelerate the process of public administration reform, and increase the transparency of the budget process.

Directors considered that the exchange rate peg had served Latvia well and remained appropriate. They generally agreed that Latvia's external position was broadly satisfactory, given the low level of external debt, the long-term nature of most of the capital inflows, and the large share in imports of capital and intermediate goods. Directors cautioned, however, that pressures on the current account deficit required close monitoring, and they welcomed the authorities' readiness to tighten fiscal and monetary policy in the event of adverse balance of payments developments.

Directors were encouraged by the increased confidence in the financial system and the steps taken by the authorities to achieve strong supervision of banks and an appropriate regulatory framework for the financial sector. They welcomed the authorities' intention to closely monitor the development of credit, and take action, if necessary, to curb credit growth and ensure the continued health of the banking system.

Directors urged the authorities to accelerate their program of structural reform in order to foster sustained economic growth and to move toward their goal of EU accession. While recognizing

that structural reforms had reached an advanced stage, Directors expressed concern about the recent slowing of some of these, and especially the recent delays in the privatization of large enterprises. They urged the authorities to give renewed emphasis to completing the privatization process. Directors also attached importance to the strengthening of property rights, and the introduction of a land registration system.

Directors encouraged the authorities to continue to strengthen their legal system and enhance transparency. In this context, they welcomed the decision by the government to publish the letter of intent.

Press Information Notices (PINs) are issued, at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

Latvia: Selected Economic Indicators

	1994	1995	1996	1997 1/
Real Economy		*In percent*		
Real GDP, annual change	2.1	0.3	2.8	6.0
CPI inflation, period average	35.8	25.1	17.6	8.4
Unemployment rate	6.5	6.6	7.2	7.0
Domestic saving, in percent of GDP	18.4	15.5	16.6	16.2
Domestic investment, in percent of GDP	20.8	18.9	20.7	23.1
Public Finance		*In percent of GDP*		
General government balance	-4.0	-3.3	-1.3	1.3
General government debt	14.5	15.3	14.2	11.2
Money and Credit		*Changes in percent*		
Reserve money	20	2	25	30
Broad money	49	3	20	39
Domestic credit to nongovernment	65	-45	1	76
One-month treasury-bill rate, in percent, per annum	20.4	30.1	10.1	3.4
Balance of Payments		*In percent of GDP*		
Trade balance	-8.2	-12.3	-14.9	-15.5
Current account	-0.2	-3.4	-4.1	-6.9
Gross international reserves (in months of imports)	4.7	3.0	3.1	3.0
Foreign direct investment, stock	6.7	10.3	16.2	22.3
Exchange Rate				
Exchange rate regime	Peg to the SDR; 0.79 LVL per SDR			
Exchange rate, lats per US$, end period	0.548	0.537	0.556	0.59

Sources: Latvian authorities; and IMF staff estimates.

1/ Preliminary.

Press Information Notice (PIN) No. 98/31
FOR IMMEDIATE RELEASE
April 27, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Malaysia

The IMF Executive Board on April 20, 1998 concluded the Article IV consultation[1] with Malaysia.

Background

Since the late 1980s, Malaysia's economy, sustained by high levels of investment and savings, and generally strong macroeconomic fundamentals, has achieved considerable success, reflected in high growth and a very substantial reduction in poverty. However, in recent years, strong demand pressures and rapid money and credit growth led to a widening of the current account deficit and sharply buoyant asset prices. Following the float of the Thai baht in July 1997, Malaysia experienced considerable pressures in its stock and foreign exchange markets. The authorities' initial response focused on supporting the ringgit through exchange market intervention and a sharp hike in short-term interest rates. Subsequently, the authorities quickly allowed the exchange rate to depreciate, lowered interest rates almost to pre-crisis levels, and introduced a series of measures. These measures included tightening fiscal policy and postponing major infrastructure projects; successively increasing constraints on credit growth and, more recently, raising interest rates; and a number of administrative actions.

However, financial markets remained volatile reflecting, in part, severe and prolonged contagion. From the second half of 1997, economic activity has slowed, and the capital account has recorded a large outflow of short-term capital. The favorable impact of exchange rate

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

depreciation on exports, combined with deliberate policies to defer nonpriority projects, have brought about a progressive and significant improvement in the current account, beginning in the second half of 1997. Reflecting the tightening of policy, monetary growth—and, latterly, credit growth—have now also slowed considerably. However, CPI inflation has picked up to 5 percent in early 1998 as the depreciation of the ringgit has fed through to prices. Gross international reserves declined by US$7 billion from end-1996 to US$20½ billion as of end-April 1998, equivalent to 3½ months of imports or 140 percent of short term debt (including payments due in 1998 on medium- and long-term debt). The ringgit depreciated by 44 percent and the stock market fell by almost 50 percent between mid-1997 and January 1998; since then, the ringgit has strengthened by about 20 percent and the stock market has recovered by 9 percent.

The weakening economy, combined with the high level of corporate leverage, also resulted in increased pressure on Malaysia's financial system, notwithstanding the generally well developed supervisory and regulatory framework. Nonperforming loans increased to 8.7 percent by February 1998, reflecting also the tightening of loan classification guidelines that took effect on January 1, 1998. In addition, in November and December 1997, there was some shift in deposits from small to large financial institutions, accompanied by segmentation in the interbank market, which required temporary liquidity injections by Bank Negara. In response, the authorities tightened provisioning and disclosure standards, accelerated mergers of finance companies, announced a deposit guarantee, and reduced the statutory reserve requirement (matched by an offsetting withdrawal of Bank Negara deposits at financial institutions) to improve liquidity flows in the interbank market; these measures also helped reverse segmentation.

In late March 1998, Deputy Prime Minister Anwar and Governor Ahmad announced a new package of measures, which builds on the earlier initiatives and is designed to broaden the overall policy response within the changed macroeconomic framework. The centerpiece is a series of preemptive actions to strengthen the financial sector and address emerging problems in financial institutions. The package also includes a rebalancing of the macroeconomic policy mix, with fiscal policy targeted at ensuring a small surplus, while increasing spending to strengthen the social safety net; a significant reduction in credit and monetary growth; and more active use of interest rates to stabilize the foreign exchange market and restrain inflation. The Deputy Prime Minister also renewed the government's commitment to improve transparency and to the steady implementation of structural measures aimed at improving corporate governance and competition. Financial markets, which had strengthened in anticipation of the package have since moderated somewhat, owing, in part, to contagion effects from weaknesses in Japan.

Executive Board Assessment

Executive Directors noted that, after a long period of rapid growth and economic transformation, the Malaysian economy had been increasingly affected by the regional crisis in Asia over the past year. However, Malaysia's relatively strong initial conditions had enabled it to avoid the most severe effects of the regional crisis. Thus, Malaysia's longstanding prudent approach to external exposure, its relatively well-developed supervisory and regulatory framework for the financial system, and a strengthening of the fiscal position had helped keep domestic and external vulnerability lower than in many other countries in the region.

Nevertheless, Directors noted that Malaysia's economy had come under considerable pressure. Growth had slowed, financial and foreign exchange markets had been volatile around a generally declining trend, capital inflows had declined, and the domestic financial system had come under stress. While contagion from the regional crisis had clearly contributed to Malaysia's economic difficulties, Directors considered that sustained rapid money and credit growth was also a contributing factor.

Directors commended the authorities for taking a succession of important measures since the middle of 1997. In particular, Directors noted that periodic attempts had been made to slow credit growth and defer infrastructure projects, while fiscal restraint had remained a cornerstone of Malaysia's economic policies. However, these measures had not been sufficient to restore confidence, in part because markets remained to be convinced of their comprehensive character and consistency. In particular, the periodic reliance on nonmarket strategies to counter financial pressures had weakened investor confidence, including in corporate governance.

Against this background, Directors welcomed the package of measures announced on March 24 and 25, 1998, which built upon previous initiatives and which constituted a proactive and much more comprehensive approach to the restructuring of Malaysia's economy. If fully and consistently implemented, Directors considered that this package would provide a strong basis for Malaysia to recover from its current difficulties and to return to more rapid rates of growth over the medium term. Directors placed particular emphasis on the tightening of monetary policy, on improvements in corporate governance and fiscal transparency, and on the early implementation of commitments to deepen structural reforms.

Directors strongly endorsed the focus on financial sector reform as the centerpiece of the adjustment strategy. While the assisted merger program for finance companies involved risks, Directors noted the inclusion of a number of safeguards, and welcomed the program's objective of consolidating the finance company sector without delay. Directors underscored the need for especially vigilant supervision of the newly created institutions, particularly with regard to their capitalization levels.

Directors endorsed the strategy to pre-emptively recapitalize the banking system, which was likely to face growing pressures over the coming year. They stressed that this should be vigorously implemented, and accompanied by the use of market-based resolution strategies, when needed, for institutions that fail to raise the necessary capital. In this context, the recent improvements in the prudential framework to achieve international best practices were welcomed. Many Directors strongly urged the early implementation of the authorities' intent to increase foreign equity investment in the financial sector, noting that it would contain the cost of recapitalizing financial institutions and help increase their competitiveness. Several Directors also encouraged the authorities to act as soon as feasible to introduce a formal deposit insurance scheme to replace the current blanket guarantee of all deposits in order to avoid a particularly strong moral hazard problem.

Directors strongly supported the authorities' proposed rebalancing of macroeconomic policies. They agreed that a reduction of the fiscal surplus, arising from the working of automatic

stabilizers, was appropriate in light of the economic slowdown. The smaller budget surplus would permit additional social safety net expenditures, which Directors believed should be targeted toward those who would be most affected by the adjustment program. In this context, they urged the authorities to scale back price controls so that they would apply only to basic food products consumed by the poorest households. Directors also supported strongly the authorities' intentions to disclose transparently and regularly all quasi-fiscal liabilities of public sector institutions—noting that such transparency had also been sought by markets—and recommended that these items be brought on budget.

Directors supported the authorities' monetary policy framework, comprising restraint over monetary growth combined with a floating exchange rate, with foreign exchange intervention limited to smoothing operations. In this context, Directors welcomed the authorities' intention to bring credit growth down from past levels of 28–30 percent, and they encouraged them to keep it close to the bottom of the 12–15 percent range. Directors stressed that a more forceful use of interest rate policy in response to possible renewed exchange market pressures was a prerequisite for market stability and an enduring return of confidence. Such a policy would also serve to help control credit growth and contain inflationary pressures.

Directors underscored the need for special emphasis on improving corporate governance and transparency, including the avoidance of bailouts of troubled corporations, which would be crucial for sustaining the recent improvements in market sentiment. To this end, they recommended the introduction of specific safeguards, including restraints on the activities of public and quasi-public institutions, and the avoidance of government guarantees. They also emphasized the importance of liberalizing limits on foreign investment, reducing barriers to entry in key sectors of the economy, and reducing tariff and nontariff barriers, all of which would serve to strengthen market mechanisms, deepen competitive forces, and revive long-term capital inflows into Malaysia. Directors also welcomed the progress achieved in reducing income inequalities in Malaysia over a long period.

Press Information Notices (PINs) are issued, at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

Malaysia: Selected Economic and Financial Indicators

	1994	1995	1996	1997 Prel.
		(Change in percent)		
Real economy				
Real GDP growth	9.2	9.5	8.6	7.8
Real domestic demand	13.9	13.6	5.3	8.3
CPI inflation (period average)	3.7	3.4	3.5	2.7
Unemployment rate (percent)	2.8	2.8	2.5	2.7
Gross national saving (percent of GDP)	32.7	33.5	36.6	38.0
Gross domestic investment (percent of GDP)	40.4	43.5	41.5	42.8
		(Percent of GDP)		
Public finance				
Federal government balance	1.4	1.3	1.1	2.6
Revenue	24.8	23.4	23.7	23.9
Expenditure and net lending	23.4	22.1	22.6	21.3
Overall public sector balance	0.9	3.7	4.8	3.3
		(Change in percent)		
Money and credit (end of period)				
M3	15.8	18.2	23.7	17.7
Domestic credit	14.3	27.7	27.4	27.1
One-month interbank rate (period average, in percent)	5.0	5.9	7.2	7.9
		(US$ billion)		
Balance of payments				
Trade balance	1.7	0.0	4.0	3.9
Exports, f.o.b.	56.6	71.7	76.8	77.8
Imports, f.o.b.	54.9	71.6	72.7	73.8
Services account balance	-6.5	-7.7	-7.7	-7.4
Current account balance	-5.6	-8.7	-4.9	-4.8
(Percent of GDP)	-7.8	-10.0	-4.9	-4.8
Capital account balance	2.5	7.0	7.4	-1.2
Medium- and long-term	4.4	6.6	5.4	6.6
Short-term	-3.2	1.0	4.1	-1.3
Portfolio capital 1/	1.3	-0.7	-2.1	-6.6
Overall balance	-3.1	-1.8	2.5	-6.0
Gross official reserves	26.6	25.1	27.7	21.7
(In months of imports)	5.8	4.2	4.6	3.5
		(Change in percent)		
International trade				
Export volume	20.9	13.1	4.2	10.7
Import volume 2/	28.2	23.1	5.0	12.1
External debt				
Total external debt (percent of GDP)	39.5	38.3	39.4	43.6
Short-term external debt (percent of total)	19.4	19.1	26.0	23.9
Debt service ratio (percent) 3/	8.9	7.2	8.7	6.3
Exchange rates				
Ringgit/US$ (end-period)	2.56	2.54	2.53	3.88
Nominal Effective Exchange Rate (1990=100, period average)	110.3	110.3	113.7	110.5
Real Effective Exchange Rate (1990=100, period average)	102.2	102.7	107.0	104.6

Source: Information provided by the Malaysian authorities; and staff estimates.
1/ Including errors and omissions.
2/ Excluding lumpy imports such as aircraft, ships, etc.
3/ Percent of exports of goods and services. Debt service includes prepayments and refinancing.

Press Information Notice (PIN) No. 98/24
FOR IMMEDIATE RELEASE
April 1, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Mali

The IMF Executive Board on December 22, 1997 concluded the 1997 Article IV consultation[1] with Mali.

Background

Following the devaluation of the CFA franc in January 1994, Mali adopted a comprehensive adjustment strategy aimed at achieving sustained economic growth and financial viability over the medium-term. Mali's efforts, which are supported by the IMF with a three-year arrangement under the Enhanced Structural Adjustment Facility (ESAF) approved in April 1996, have resulted in significant improvements in a number of areas, including per capita GDP growth, a decline in inflation, and a reduction in internal and external imbalances.

Over the last three years, real GDP growth averaged about 4 percent a year, and real per capita income has been rising. This reflects strong increases in agricultural production, especially of cotton, a vigorous expansion in the mining sector and continued robust growth in services, including commerce. Recent indications suggest that these trends are continuing in 1997, with the coming on stream of a new gold mine, and further gains in agricultural output.

Inflation, based on the consumer price index (CPI) for Bamako, declined from about 32 percent in 1994 to less than 3 percent in 1996, and remained low and stable during the first half of 1997. The CPI-based real effective exchange rate is estimated to have depreciated by about

[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

1.5 percent in 1996, compared to 1995, and by 4 percent in the first half of 1997, contributing to a further improvement in the competitiveness of the Malian economy. The external current account deficit was reduced from about 17 percent of GDP in 1994 to less than 15 percent in 1996. There were continued strong increases in export volumes, especially cotton fiber, while import volumes, dominated by capital goods and equipment, expanded at a more moderate pace over the same period.

The overall fiscal deficit (on a commitment basis and excluding grants) was reduced from 13¾ percent of GDP in 1994 to 7.9 percent in 1996 through the authorities' continued efforts to increase revenues, while restraining nonpriority current spending. Measures to strengthen tax and customs administrations, enlarge the tax base, and improve compliance contributed to raising the tax revenue to GDP ratio to almost 13 percent in 1996, from 10 percent in 1994. Over the period, total government expenditure was reduced by 3.5 percent to 24 percent of GDP, through the containment of the wage bill and lower-than-expected interest payments on external debt. At the same time, spending on basic education and primary health services, reached some 25 percent of total outlays in 1996.

Broad money is estimated to have increased by 12 percent in 1996, in line with nominal GDP. Credit to the economy rose by 29 percent, reflecting private sector financing of activity in the construction, industry, and the mining sector. Reflecting the easing of interest rates abroad, the Central Bank of West African States, which conducts monetary policy at the regional level, lowered the discount rate, and the banks' average prime lending rate declined, from 13 percent in 1994 to about 9 percent in 1997.

On the structural front, some progress have been made in promoting private sector development, restructuring public enterprises and implementing agricultural reforms. However, delays were incurred in the implementation of a number of structural reforms as some of the public enterprises slated for privatization failed to attract buyers, and the financial audit needed to prepare for the sale of a tobacco company was not completed on time.

Developments thus far in 1997 suggest that real GDP could increase by close to 7 percent, bolstered by strong growth in gold production and a record cotton crop. Inflation is expected to remain in the 2-3 percent range. The overall fiscal deficit (excluding grants) is expected to be in line with initial projections at about 9 percent of GDP. The external current account deficit (excluding official transfers) could narrow by close to 4 percentage points of GDP to 11 percent, due to sharp increases in cotton fiber and gold exports.

Despite these achievements, Mali remains one of the low-income countries with the weakest social indicators including low life expectancy, low primary school enrollment, and high illiteracy rate.

Executive Board Assessment

Executive Directors agreed with the thrust of the staff appraisal. They were encouraged by developments during the first half of 1997 and under the second annual ESAF-supported

program, with real GDP growing faster than projected and inflation declining further. However, Directors emphasized the importance of strengthened adjustment efforts, in particular, in the areas of fiscal consolidation, structural reforms, and the promotion of the private sector, in order to strengthen economic performance, to reduce vulnerability to shocks, and to address poverty concerns.

In the fiscal area, Directors hoped for a speedy adoption of the draft supplementary budget by the National Assembly. Noting the expenditure overruns in the first half of 1997 associated with the recent elections and the shortfall in external assistance, this measure would help address these overruns and ensure the attainment of the original program fiscal target for 1997.

Directors stressed that the fiscal situation remains fragile and that there is a need to improve the revenue situation. In particular, with the impending move toward a common external tariff in the West African Economic and Monetary Union during the period 1999–2000, the authorities should be prepared to offset any adverse impact of the tariff reform on government revenue. In this regard, early steps should be taken to expand the tax base through decisive reductions in tax and customs duty exemptions, the unification of the VAT rates, and the extension of the duty drawback system—introduced in 1997 for imports of petroleum products—to other duty-exempt imports. The revenue collection agencies should also be strengthened through the provision of adequate material and human resources. On the expenditure side, Directors noted that part of the social safety net allocations had been used to finance the elections. They urged the authorities to supplement the steps already taken to partially restore the social safety net allocations by additional measures to increase such allocations under the 1998 budget. They also encouraged the authorities to continue their policy of restraint on overall spending, particularly with regard to the wage bill, and ensure that more resources are allocated to education and health expenditures.

Directors welcomed the full repayment of central bank refinancing by end-October, noting that such instances of quasi automatic central bank refinancing to banks could undermine the development of an effective interbank market. Directors emphasized that the regional central bank should rely mainly on the use of indirect monetary instruments and refrain from market interventions aimed at accommodating bank-specific liquidity needs, and take steps to ensure that its refinancing ('pension') rate remains above the yield on alternative short-term funds. Directors welcomed the improvements in the health of the banking system in recent years, and encouraged the Malian authorities to take all necessary steps to enable commercial banks to recover bad loans and to promote the competitiveness of the financial sector. They urged expeditious restructuring of Banque Internationale du Mali and the privatization of Banque Malienne de Credits et de Depôts.

Directors expressed concern about the relatively slow progress in implementing the structural reform program, and stressed the need for an intensification of reforms, given their critical importance for improving the environment for private sector activity and diversifying the export base. In this context, Directors urged the Malian authorities to review the present institutional framework for public enterprises, including an in-depth assessment of the merits of continued government ownership of a large number of enterprises, and to strengthen the management of

such enterprises. Directors were of the view that enlarging the privatization program to include most of the enterprises still in the government's portfolio, and in particular the cotton marketing company (CMDT), the electricity and water company (EDM), and the telecommunications company (SOTELMA), would contribute to strengthening the country's growth prospects to a level that can help reduce poverty.

Directors noted that the judicial system appears unable to enforce contracts and protect private property rights, and urged the authorities to take steps to overhaul the system, starting with the commercial courts, and ensure a more balanced representation of all economic and financial interests.

Directors encouraged the authorities to step up their efforts to improve the coverage, consistency, and availability of the core economic indicators required for surveillance and program monitoring. In this regard, Directors pointed to the usefulness of technical assistance and the need to implement technical assistance recommendations.

It is expected that the next Article IV consultation with Mali will be held on the standard 12-month cycle.

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Mali: Selected Economic Indicators

	1993	1994	1995	1996 Prel.	1997 Proj.
	Annual percentage change				
Domestic Economy					
Real GDP	-2.4	2.3	6.4	4.0	6.7
GDP deflator	2.6	33.2	12.5	6.3	1.8
Consumer prices	0.4	32.0	9.2	2.8	2.6
	In percent of GDP				
Gross fixed investment	21.9	26.0	26.0	26.5	25.8
Gross domestic savings	6.4	7.1	9.5	10.8	14.2
Gross national savings	9.0	9.1	10.7	11.8	15.0
	In millions of U.S. dollars 1/				
External Economy					
Exports, f.o.b.	349.3	336.5	452.3	446.3	545.7
Imports, f.o.b.	677.9	629.2	796.4	797.1	781.0
Current account deficit (excluding grants)	-344.8	312.8	-377.2	-390.9	-279.4
Capital account	-24.7	82.4	122.4	140.9	99.3
Overall balance	5.3	122.5	67.7	127.6	-12.2
Current account deficit (in percent of GDP)	-12.9	-16.9	-15.3	-14.7	-10.8
Debt service (in percent of exports of goods and nonfactor services) 2/	39.6	41.8	31.6	29.3	25.0
Debt service (in percent of government revenue) 2/	72.0	67.8	47.3	36.3	38.7
External debt (in percent of GDP)	109.9	135.8	113.3	113.6	113.9
Real effective exchange rate (end of period; percent change) 3/	-2.0	-38.1	12.6	3.6	...
	In percent of GDP 1/				
Financial Variables					
Government revenue	13.9	13.5	14.4	15.9	15.5
Total expenditure	23.5	27.2	24.9	23.4	24.3
Overall fiscal deficit (commitment basis, excluding grants)	-9.6	-13.7	-10.5	-7.9	-8.8
Change in broad money (in percent)	8.4	39.1	19.6	11.9	7.6

Sources: Malian authorities; and IMF staff estimates and projections.

1/ Unless otherwise specified.
2/ Before debt rescheduling, but after debt cancellation.
3/ Minus sign indicates depreciation of the CFA franc.

Press Information Notice (PIN) No. 98/23
FOR IMMEDIATE RELEASE
March 31, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Morocco

The IMF Executive Board on March 6, 1998 concluded the 1997 Article IV consultation[1] with Morocco.

Background

Morocco's economic growth in the 1990s has been dampened by recurring droughts, and annual growth of the nonagricultural sector declined from 3.9 percent in 1979–90 to 2.8 percent in 1991–97. Following a record cereal crop leading to a 12 percent increase in real GDP in 1996, agricultural output suffered from adverse weather conditions in 1997 and total GDP contracted by 2.2 percent even though nonagricultural sectors expanded by about 3 percent. While unemployment declined in 1997, it still remains high at 16.6 percent.

Tight demand management contributed to reducing inflation further, from 3 percent in 1996 to 1 percent in 1997, consistent with maintaining a nominal exchange rate anchor. Interest rates declined with the rate on one-year treasury bills falling from 9 percent to 7 ½ percent. The stock market rose by 48 percent in 1997, largely unaffected by the recent turbulence in Asia. Privatization was a major success in 1997 (1.4 percent of GDP in receipts) and foreign direct investment exceeded expectations (3.5 percent of GDP).

In the fiscal year 1996/97 (July-June), the central government overall deficit (excluding privatization receipts) was reduced to 3.2 percent of GDP. Revenues reached 24.8 percent of

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

GDP, substantially exceeding the objectives of the budget. Expenditure levels were lower than budgeted, reflecting lower capital outlays, interest payments and other nonwage current spending. However, the wage bill increased (by 0.3 percent of GDP) beyond the budgeted amount, reflecting the agreements reached by the government with employers and trade unions in the context of the "Social Dialogue" held during the summer of 1996.

In 1997, Morocco's external current account deficit contracted to 1.1 percent of GDP, from 1.7 percent of GDP in 1996. Export volume picked up in 1997 (4.9 percent), driven in particular by phosphates and its derivatives, textiles and pharmaceuticals. In the capital account, direct foreign investment increased from US$0.4 billion to US$1.2 billion on the strength of an improved climate for private sector activity and the sale of public enterprises to foreign investors. These inflows enabled Morocco to raise its official reserves to US$4 billion (4.5 months of imports of goods and nonfactor services) and, together with an active debt management policy, to reduce the stock of its external debt as well as its average cost.

In recent years structural reforms have concentrated on improving the environment for stronger private sector-led growth, and addressing weaknesses in the social sectors. Particular emphasis was put on upgrading the judicial system, restructuring the financial sector, reorienting education toward basic instruction and higher enrollment, and simplifying the regulatory environment. The legal basis for private sector development was further strengthened by amendments to the corporate laws and bankruptcy procedures.

Executive Board Assessment

Executive Directors commended the Moroccan authorities for the progress made over the past two years in macroeconomic stabilization and in liberalizing the economy, despite the economic and social impact of the recurring droughts. Directors noted that the strong budget execution during 1996 and the 1996/97 fiscal year, and prudent monetary and exchange rate policies, had contributed to lowering price inflation to levels prevailing in advanced economies, strengthening the external position, rebuilding official reserves to comfortable levels, and reducing the external debt. Nevertheless, Directors observed that Morocco's growth record in the 1990s had fallen short of expectations and remained below potential. Thus, Directors emphasized the importance of accelerating the pace of structural reforms, including in the social sphere, so as to strengthen social cohesion and further develop a qualified labor force.

Directors emphasized that fiscal consolidation should be given high priority in the short term as well as over the medium term. They considered that the projected widening in the budget deficit in 1997/98, due mostly to the salary increase that had been granted in 1996 as part of the "Social Dialogue," was not consistent with the need for stronger fiscal consolidation. They urged the authorities, starting with the 1998/99 budget, to strengthen their efforts to attain fiscal consolidation over the medium term so as to raise savings and achieve higher growth. Regulatory and tax administration reforms had produced strong results in the past fiscal year. However, in the period ahead, Directors encouraged the authorities to consider various expenditure measures, including steps to reduce Morocco's government wage bill, civil service

reform, and replacing food subsidies with better targeted assistance. Directors also noted that there was scope to increase revenues through indirect taxes, such as the value-added tax, as suggested by recent Fund technical assistance missions.

Directors agreed that the use of the exchange rate as a nominal anchor had been effective over the past few years in enforcing fiscal discipline, reducing inflation, and in encouraging the private sector to make sustained efforts at raising its productivity and competitiveness. While a few Directors saw merit in contemplating an early shift to a more flexible regime, most Directors agreed with the authorities' view that adopting a more flexible arrangement at this time would be premature, as they felt that the necessary preconditions were not yet in place. Directors argued that the authorities should continue to aim at improving competitiveness, including through strengthened structural reforms and an increase in productivity. It was also emphasized that increasing exchange rate flexibility would require that a solid alternative mechanism for controlling inflation be in place. Directors generally agreed that the authorities should continue to closely monitor developments and the appropriateness of the exchange rate regime, taking into account the external position and the competitiveness of the economy.

Regarding structural reforms, Directors commended the authorities for the measures already undertaken, and specifically for addressing rigidities in the regulatory environment, establishing commercial courts, and simplifying judicial procedures. They also called for early action in completing the process of price liberalization, and increasing labor market flexibility through the adoption of a new labor code. This was seen as essential for reducing unemployment and undertaking the large-scale reallocation of resources necessary for Moroccan enterprises to enhance their competitiveness and reorient their production toward more dynamic markets. In this respect, a few directors cautioned the authorities about minimum wage trends, which may have negative employment effects.

Directors welcomed the measures taken to liberalize Morocco's financial system and strengthen the prudential control of the banking system, which appears to be well prepared to play a more active role in the future. Directors encouraged the authorities to take further steps to encourage greater competition, pointing out the opportunities provided in this regard by the planned privatizations, as well as by the modernization of the national savings bank and the postal checking system. They also advocated continued efforts aimed at improving financial supervision.

Directors welcomed the authorities' broad range of measures toward improving social conditions in Morocco, in particular the pragmatic approaches to raise school enrollment and to strengthen basic health services in rural areas. However, given the need to rapidly enhance Morocco's human capital to sustain productivity growth, Directors urged the authorities to reform the education system and redouble their efforts at improving the skill mix and at raising the literacy rate so as to obtain dramatic results in a relatively short period of time.

Directors welcomed Morocco's efforts to improve the quality and timeliness of economic and financial data, and to increase availability of these data to the broader public. Directors

encouraged the authorities to continue these efforts, particularly in light of their intention to subscribe to the Special Data Dissemination Standard.

Press, Information Notices (PINs) are issued, at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

Morocco: Selected Economic Indicators

	1994	1995	1996	1997
Domestic economy		In percent		
Change in real GDP	10.4	-7.0	12.0	-2.2
Nonagricultural GDP	2.6	1.9	3.3	3.1
Unemployment rate	20.3	22.9	18.1	16.6
Change in consumer prices	5.1	6.1	3.0	1.0
External economy		In billions of U.S. dollars 1/		
Exports f.o.b.	5.5	6.9	6.9	6.9
Imports f.o.b.	7.6	9.3	9.0	8.9
Private transfers	2.1	2.2	2.4	2.1
Current account balance	-0.7	-1.5	-0.6	-0.4
In percent of GDP	-2.4	-4.6	-1.7	-1.1
Direct investment	0.8	0.3	0.4	1.2
Public borrowing, net	-0.3	-0.2	-0.3	-0.7
Capital account balance	1.3	0.9	0.8	0.6
Gross official reserves	4.3	3.6	3.8	4.0
Financial variables		In percent of GDP 1/		
Central government balance 2/	-3.9	-5.6	-3.7	-3.2
Central government debt	82.4	83.1	75.4	78.5
of which external	48.8	46.9	40.8	39.4
Debt service ratio (in percent of exports of goods and nonfactor services)	32.6	31.8	28.2	25.4
Change in broad money (in percent)	10.2	7.0	6.6	8.2
Interest rate 3/	8.5	9.0	9.0	7.5

Sources: Data provided by the Moroccan authorities; and IMF staff estimates.
1/ Unless otherwise noted.
2/ Commitment basis, excluding privatization receipts, 1997 column refers to the 1996/97 fiscal year.
3/ 52-week treasury bills.

Press Information Notice (PIN) No. 98/33
For Immediate Release
April 30, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Mozambique

The IMF Executive Board on April 7, 1998 concluded the Article IV consultation[1] with Mozambique.

Background

After a difficult period in which the Mozambican economy suffered as a result of civil war and weak economic policies, in 1987 the government launched an Economic Rehabilitation Program (ERP) supported by the IMF. The program involved a fundamental shift to market-based economic policies and structural reforms. Major reforms undertaken since then include the unification and stabilization of the exchange rate; significant tariff reforms and trade liberalization; the elimination of most price controls; the privatization of about 900 public enterprises; and extensive financial sector reforms. Under the ERP, Mozambique has made impressive economic gains: real GDP and exports grew on average by 6.8 percent and 15.6 percent, respectively, in the 1987-97 period. Nevertheless, Mozambique remains a relatively poor country with social indicators that are below the average for sub-Saharan African countries.

Real GDP growth in 1997 was provisionally estimated at 7.9 percent, which is higher than the program forecast and the highest level in four years. Growth was broad-based, with transportation, industry, and services showing particularly encouraging outcomes. Agriculture grew by 5.9 percent, with a decline in cashew, but a strong increase in cotton (43 percent) and foodstuffs (22 percent). Good weather, prudent financial policies, and an increase in private investment linked to privatization explain the rising activity level. Inflation was 5.8 percent in 1997 (end of period), or less than half of the program target (14 percent) and the lowest inflation rate since

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

independence in 1975. Inflation has declined steadily from 70 percent in 1994 as a result of greater monetary control, exchange rate stability, and the strong supply response in the economy.

Monetary expansion was 25 percent in 1997, faster than the program target of 20 percent, despite the fact that base money expanded by 16 percent only and remained well within its target for the year. Two factors explain the faster than programmed monetary expansion. First, money demand was higher than expected spurred by the more dynamic economy, increased confidence, and high real interest rates for deposits. Second, the money multiplier increased owing to a decline in the currency to deposits ratio and because of a shift toward time deposits, which are not subject to reserve requirements. The Bank of Mozambique accommodated the higher money demand by allowing credit to the economy to increase 21 percent more than programmed and by accumulating net foreign assets in excess of targets. This action avoided the negative effect on growth that might have resulted had the original monetary targets been observed.

The overall deficit before grants increased from 17.0 percent of GDP in 1996 to 20.1 percent in 1997, as foreign aid (grants and concessional loans) expanded. Total revenue increased from 18.0 percent in 1996 to 20.4 percent in 1997, owing mainly to a rise in tax revenue from 16.5 percent of GDP in 1996 to 18.9 percent in 1997. The increase in tax revenue stemmed from a strengthening of tax and customs administration, as well as from the quarterly adjustment of the petroleum tax rates. Total expenditure and net lending grew by 5.5 percent of GDP from 1996 to 1997, with current expenditure increasing from 15.9 percent of GDP in 1996 to 18.9 percent in 1997 and capital expenditure rising from 18.9 percent of GDP in 1996 to 21.5 percent in 1997. Current expenditure in health and education increased in real terms, while the growth in capital expenditure reflected primarily higher spending on transportation and the water sectors.

Merchandise exports increased from US$226 million in 1996 to US$234 million in 1997. The growth of merchandise exports other than cashews was much stronger, about 14 percent. Nontraditional exports and, in particular, apparel are expanding at rapid rates. The surrender requirement on exports proceeds was eliminated in January 1997. Imports declined by 1 percent to US$775 million in 1997, owing to import substitution. Gross international reserves of the Bank of Mozambique increased to more than six months of imports at end-December 1997. The metical depreciated by only 4 percent in 1996 and less than 2 percent in 1997. The spread between the market and the parallel exchange rate has narrowed to less than 2 percent in the first quarter of 1998.

Mozambique continues to make significant progress in several structural reform areas. Customs management was privatized in 1997 and a system of full reconciliation of import taxes due and taxes paid was set up, preparations are underway for the introduction of the value added tax, new budgetary recording and monitoring procedures have been introduced, public administration is being decentralized, and a civil service reform is being finalized for implementation in 1999. The privatization program is on track for completion in mid-1999, the legal and regulatory framework is being restructured to facilitate trade and investment, and labor legislation is being updated. The last remaining state-owned bank was privatized in September 1997, commercial bank accounting procedures were updated, a new Financial Institutions Law has been submitted to the Assembly of the Republic, and banking supervision is being strengthened. A series of steps were taken to prepare the introduction of indirect monetary policy instruments. Bank reserve requirements were

lowered, extended to foreign currency deposits, and made more flexible; an interbank money market was established in September 1997; and the payments system is being modernized.

In September 1997 the Executive Boards of the IMF and the World Bank decided in their preliminary discussions that Mozambique qualified for assistance under the HIPC Debt Initiative. The Initiative is a key to reducing the debt burden to sustainable levels and to freeing resources to finance critical structural and social reforms. On April 7, 1998 the Executive Board of the IMF agreed that Mozambique had reached the decision point under the Initiative, and that the completion point would be reached in mid-1999. Together with a similar decision by the IDA Board also on April 7, 1998, this means that Mozambique now qualifies for interim assistance under the Initiative.

Executive Board Assessment

Executive Directors noted that the Republic of Mozambique's overall economic performance had continued to improve in 1997, as evidenced by higher growth, falling inflation, an improvement of the external current account, and the stability of the nominal exchange rate. These positive developments had further bolstered confidence, and private investment was on the upswing.

Directors commended the authorities for adhering to their macroeconomic program for 1997/98, as well as for their determined efforts to implement the wide-ranging structural reforms set out in the policy framework paper. Most Directors agreed that the unexpectedly strong money demand and the need to avoid slowing growth had warranted the somewhat higher than programmed monetary expansion, especially as it appeared to have no adverse impact on prices. However, they advised the authorities to closely monitor economic developments and to take quick action to curtail money and credit growth if there are signs of overheating.

Directors noted that, despite the recent economic gains, Mozambique still faced major economic problems, notably widespread poverty, an inadequate social and economic infrastructure, and a heavy external debt burden. They stressed the need for firm adherence to the program, through continued prudent financial management and an acceleration of the remaining structural reforms, in order to consolidate the gains already achieved and to place the economy on a path of strong and sustainable growth.

In this context, Directors endorsed the proposed policy framework for 1998. They observed that the continued heavy dependence on foreign aid indicated a need to raise public sector savings, boost export growth, and increase financial deepening. Directors welcomed the significant strengthening of tax revenues in 1997, and urged the authorities to maintain or increase the momentum of improvements in tax and customs administration and to broaden the tax base. They recommended an early introduction of a value-added tax, to be accompanied by a public information program. They also urged the authorities to undertake a review of the pension system in order to reduce the burden of pension payments on the budget. Directors welcomed the introduction of a new budgetary accounting framework, which would further enhance budgetary transparency and facilitate a reallocation of resources to social programs.

Several Directors stressed that the authorities should pay attention to the efficiency—as well as the level—of investment, the absorptive capacity constraints facing the economy, and the

implications of higher investment spending for recurrent costs. They agreed that an improvement in aid coordination would help achieve better resource allocation, and advised the authorities to continue their discussions with donors to resolve the outstanding issues.

Directors welcomed the near-completion of the privatization program and the efforts to restructure the remaining public enterprises. They encouraged the authorities to consider full privatization of the remaining enterprises under the program. They also urged the authorities to give high priority to the reforms of public administration and the pension system.

Directors noted the high level of dollarization of the economy. Directors emphasized the importance of maintaining prudent monetary policies, adequate bank supervision, and a prudent level of gross international reserves. While noting that the evidence on external competitiveness is mixed, Directors cautioned that a further real effective appreciation of the metical should be avoided.

A few Directors were disappointed by the slower progress toward trade reform in the most recent period. The authorities were encouraged to further reduce tariff spreads and exemptions. Directors also suggested that the recently signed free trade protocol with the Southern African Development Community (SADC) could provide an added opportunity to set more ambitious trade reform objectives. Directors also encouraged the authorities to accept the obligations of Article VIII, Sections 2, 3, and 4 within the year.

Directors also considered the final document on the Heavily Indebted Poor Countries (HIPC) Initiative for Mozambique. They agreed that Mozambique is eligible and qualifies for assistance under the HIPC Initiative. The consensus view was that the completion point should be in June 1999, subject to the conclusion of the midterm review under the third annual arrangement under the current three-year enhanced structural adjustment arrangement, and approval of a new three-year enhanced structural adjustment arrangement by that date. They welcomed the exceptional efforts that are to be made by all of Mozambique's creditors in a spirit of equitable burden sharing. They also agreed that the external debt sustainability target for the net present value of the debt-to-exports ratio for Mozambique at the completion point will be 200 percent and the target of the debt-service-to-exports ratio will be 20 percent. Directors emphasized that access to enhanced debt relief under the HIPC Initiative was conditional upon satisfactory implementation of a strong program of structural reform and actions in the social area.

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Mozambique: Selected Economic Indicators, 1994-98

	1994	1995	1996	1997	1998 Proj.
			(In percent)		
Domestic economy					
Change in real GDP	4.5	1.4	6.2	7.9	9.4
Change in consumer prices (end of period)	70.2	54.1	16.6	5.8	6.0-10.0
			(In millions of U.S. dollars)[1]		
External economy					
Exports, f.o.b.	164	174	226	234	325
Imports, f.o.b.	881	727	783	775	965
Current account balance[2]	-300	-338	-359	-260	-453
Direct investment and project grants	333	274	296	335	365
Capital account balance	-10	64	237	162	196
Current account balance (percent of GDP)[2]	-20.5	-22.7	-20.6	-13.4	-20.9
Change in real effective exchange rate (in percent; +appreciation)	-3.2	-4.4	14.9	14.7	...
			(In percent of GDP)[1]		
Financial variables					
Gross national savings	30.5	28.5	27.5	31.8	31.4
Gross domestic investment	51.0	51.2	48.2	45.2	52.3
Central government balance (before grants)	-29.7	-20.8	-17.0	-20.1	-19.4
Primary balance	-28.0	-17.4	-14.4	-17.6	-16.5
Change in broad money (in percent)	57.6	54.7	21.1	25.4	22.2

Sources: Data provided by the Mozambican authorities; and IMF staff estimates.

[1]Unless otherwise indicated.
[2]Including grants.

Press Information Notice (PIN) No. 98/1
FOR IMMEDIATE RELEASE
January 12, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with New Zealand

The IMF Executive Board on November 7, 1997 concluded the 1997 Article IV consultation[1] with New Zealand.

Background

Over the past decade, innovative policy reforms have resulted in an outward-oriented, competitive, and dynamic economy. Since 1991, GDP has grown by an average of 3½ percent per annum, unemployment has been reduced from 10½ percent to 6¾ percent, and inflation has been kept close to 2 percent. Further, the government operating budget has been in surplus for four consecutive years, reducing net debt by half, to 27 percent of GDP.

During 1995 and 1996, the prolonged expansion, together with unexpected shocks, caused underlying inflation to breach the ceiling of the 0–2 percent target band. In response, the Reserve Bank moved to reinforce an already tight monetary policy stance. High real interest rates and a sharp appreciation in the New Zealand dollar have resulted in underlying inflation declining from an annual rate of 2.4 percent in December 1996 to 1.8 percent in September 1997. Meanwhile, output growth has slowed, to an annualized rate of only 1½ percent in the first half of 1997, as private investment and consumption—the motors of the expansion—decelerated, and output has now fallen slightly below its potential. Employment growth has also stagnated, and the unemployment rate has risen to 6¾ percent, from 6 percent at the end of 1996.

Despite the slowdown in domestic activity, the current account deficit has widened markedly, to

[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

6½ percent of GDP (national definition) in the June 1997 year. Three factors have been responsible: the goods and services surplus has declined as the exchange rate has appreciated and competitiveness has deteriorated; the investment income deficit has risen as payments on external liabilities have increased significantly and earnings on New Zealand's overseas assets have fallen; and migrant transfers have declined following a tightening of immigration policy.

In December 1996, the inflation target band was widened to 0–3 percent, and the Reserve Bank refocused its policy on the new 1½ percent inflation point target. With inflationary pressures declining, the Reserve Bank has been able to ease monetary conditions since the beginning of the year. This has occurred mainly through the exchange rate, with the real effective rate depreciating by 6 percent during April–September, although it still remains above its longer-term trend. Short-term interest rates have also fallen, but remain above 6 percent in real terms.

The fiscal surplus has narrowed from 3½ percent of GDP in the 1995/96 fiscal year (July–June), to 2 percent in 1996/97. While part of this reflected the cyclical slowdown, there was also a structural deterioration as income taxes were cut (by the equivalent of 1 percent of GDP). The 1997/98 budget projected a further decline in the surplus to 1½ percent of GDP. This reflects, in part, a further decline in the structural budget position in response to increased expenditures on health, education, and pensions.

Executive Board Assessment

Executive Directors commended the authorities for implementing rigorous macroeconomic policies and innovative reforms, including a transparent macroeconomic policy setting process and public sector accounting framework, that had transformed the economy into one that is outward-oriented and dynamic. For the past several years New Zealand has been reaping the benefits of reforms—economic expansion has been generally robust, the unemployment rate is among the lowest in the industrialized world, and inflation is low.

Directors observed that the economy is now facing several challenges. Growth has slowed, the structural fiscal surplus has been reduced, private savings is low, competitiveness has deteriorated, and the current account deficit has widened. While noting the continuing international confidence, Directors considered that the sizable external imbalance posed risks, given New Zealand's already high stock of external liabilities and its vulnerability to external shocks. Directors generally believed that it would be advisable for the authorities to tighten policies to minimize the risks, particularly in light of current regional uncertainties, with a number of Directors considering that fiscal tightening could be achieved by scaling back medium-term expenditure plans. A tighter fiscal position would also enable a more balanced policy mix and allow the monetary stance to be eased somewhat further, alleviating the strain on the export sector.

Directors noted that the aging of the population would put pressure on the fiscal position over the longer term, and commended the authorities for their forward-looking efforts to meet those pressures. Noting the recent referendum result rejecting the government's proposal to privatize the pension system, Directors encouraged the early consideration and implementation of

measures to reduce the fiscal cost of the public pension scheme, noting that a number of possibilities had been under discussion in New Zealand, including raising the retirement age, reducing the replacement rate, and means-testing benefits. Directors also noted the advantages of moving quickly to implement the health-care reform policy, and hoped that it would provide more scope for competition between the public and private sectors.

Directors observed that the current monetary policy framework has successfully maintained price stability. In particular, the requirement that the Reserve Bank bring inflation back to target quickly, following deviations from a narrow target band, has built credibility and reduced inflation expectations. A number of Directors agreed with the staff that there might be scope to adopt a more gradualist approach to correcting inflation deviations, so as to better allow for the long lags of monetary policy; but Directors also cautioned that this approach must be supported by an appropriate fiscal policy, to preserve credibility. Some other Directors believed that the current approach taken by the Reserve Bank was appropriate. Directors thought that the recently adopted monetary conditions index provided a useful additional signaling device, but cautioned that it should not be used as a rigid intermediate target.

Directors endorsed the authorities' efforts to raise potential growth by improving educational quality, encouraging labor force participation, and further deregulating the economy. However, the level of dependency on government benefits remains high, and Directors encouraged further efforts to tighten eligibility criteria and to enhance incentives for work. Directors also called for a careful review of government support for the monopoly agricultural export boards, as deregulation could improve export competitiveness. In that context, some Directors noted the need for the liberalization of agricultural trade in other countries.

Press Information Notices (PINs) are a new series of IMF press notices (see Press Release 97/21). PINs are issued, at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

New Zealand: Selected Economic and Financial Indicators

	1991	1992	1993	1994	1995	1996	Proj. 1997
Real Economy			*Change in percent 1/*				
Real GDP (production basis)	-1.7	0.9	5.0	6.0	3.6	2.8	1.9
Consumer Price Index (headline)	2.6	1.0	1.3	1.8	3.8	2.3	1.0
Consumer Price Index (underlying)	2.5	1.5	1.6	1.2	2.0	2.3	1.6
Unemployment rate (in percent)	10.3	10.3	9.5	8.1	6.3	6.1	6.8
Investment (in percent of GDP)	15.7	17.3	19.9	21.5	22.0	21.6	21.8
National savings (in percent of GDP)	13.9	15.9	18.0	18.3	18.5	17.7	15.4
Public Finance 2/			*In percent* of GDP				
Operating balance	-7.0	-1.1	0.9	3.1	3.7	2.0	1.5
Revenue 3/	37.4	40.5	37.1	38.1	38.6	37.1	36.6
Expenditure	44.5	41.6	36.2	35.0	35.0	35.0	35.0
Money and Credit			*Change in percent*				
Private sector credit	2.8	14.2	9.1	8.2	14.2	11.8	10.0 4/
M3	6.9	10.7	5.4	3.5	15.6	11.3	7.1 4/
Interest Rates			*In percent, annual average*				
90-day bank bill	10.0	6.7	6.3	6.7	9.0	9.3	8.1 5/
10-year government bond	9.9	8.4	6.8	7.6	7.8	7.9	6.9 5/
Balance of Payments			*In billions of New Zealand dollars* 1/				
Trade account	3.6	3.0	3.2	2.3	1.4	0.7	1.0
Exports	16.6	18.1	19.4	20.2	20.5	20.6	22.1
Imports	13.0	15.1	16.1	17.9	19.2	19.9	21.1
Current account	-1.6	-2.0	-0.9	-2.1	-3.3	-3.8	-6.3
(In percent of GDP)	(-2.2)	(-2.7)	(-1.2)	(-2.5)	(-3.7)	(-4.1)	(-6.5)
Official reserves	5.5	6.0	6.0	5.8	6.8	8.4	6.7 4/
Gross External Debt 6/			*In percent of GDP, end of period*				
Official debt	27.8	31.6	32.6	27.4	24.3	22.1	...
Total debt	86.0	91.8	90.0	81.2	80.3	80.8	...
Exchange Rate			*Year average*				
Exchange rate regime:	Freely floating						
US$/$NZ	0.579	0.538	0.541	0.594	0.656	0.688	0.636 5/
TWI (June 1979=100)	57.6	53.7	54.9	57.2	61.1	65.6	64.5 5/
Nominal effective exchange rate (1990=100)	97.1	88.9	93.7	100.2	105.2	113.0	116.4 4/
Real effective exchange rate (1990=100)	95.5	85.7	89.0	94.2	99.8	108.6	110.6 4/

Sources: Data provided by the New Zealand authorities; IMF, *International Financial Statistics*; and Fund staff projections.

1/ Unless indicated otherwise.
2/ Fiscal year beginning July 1. Data for 1997 are from the 1997/98 budget.
3/ Includes surplus attributable to state-owned and Crown entities.
4/ July 1997.
5/ September 1997.
6/ Data for March of the following year.

Press Information Notice (PIN) No. 98/27
FOR IMMEDIATE RELEASE
April 9, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Nicaragua

The IMF Executive Board on March 18, 1998 concluded the 1997 Article IV consultation[1] with Nicaragua at the same time it approved the authorities' request for a three-year arrangement under the Enhanced Structural Adjustment Facility (see Press Release No. 98/7).

Background

Following a decade of civil war, public sector overexpansion and hyperinflation, Nicaragua changed its course drastically during 1990-97 as peace was reestablished and substantial progress in policy implementation was made to reduce macroeconomic imbalances and to transform to a market-based economy. Macroeconomic policies were strengthened, most price controls eliminated, and the foreign exchange and trade systems liberalized. A program of public asset divestment was implemented, and public employment and military outlays declined substantially. Private banks were allowed to operate again and the Superintendency of Banks was created as an independent unit.

As a result, **inflation** was reduced dramatically to single digits in 1997, and **real GDP** growth resumed in 1994 and accelerated to around 5 percent by 1997. During 1993–97, domestic investment (mainly public sector) rose markedly and was financed to a large extent by sizable concessional external financing. While the rate of **unemployment** fell below 14 percent in 1997 (from 22 percent in 1993), Nicaragua remains one of the poorest and most heavily indebted countries in the Western Hemisphere. Moreover, the public finances remained weak and in

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combination with a loosening of credit controls, led to pressures on net official international reserves.

The objectives of the authorities' medium term strategy for 1998–2000 are to move the economy toward sustainability of the public finances and the external sector, structural reform, and economic growth in order to alleviate poverty and reduce unemployment. The macroeconomic objectives for 1998–2000 are to: (1) increase gross international reserves—net of central bank paper, CENIS—to the equivalent of 3 months of imports; (2) bring down inflation to about 5 percent; and (3) achieve a rate of real GDP growth of around 6 percent a year.

Achieving these objectives requires the strengthening of macroeconomic policies and the resumption of structural reforms. The **fiscal program** aims at reducing the size of the public sector. Public savings would rise from 3.5 percent in 1997 to 8 percent in 2000 and the combined public sector deficit (after grants) would shift to a small surplus by 2000. Policies include a tax reform, introduced in 1997, tight control of outlays, and improved performance of public utilities and social security. The central bank will conduct a tight **credit policy**. Directed credit was eliminated in late 1997; all branches of the largest state bank have been sold or closed; and, reserve requirements have been strengthened and broadened. The **structural program** aims at broadening the scope for private sector activity through privatization of public enterprises and state banks, reforms of the public sector, strengthening property rights, a comprehensive judicial reform, and improving prudential regulation and banking supervision.

Executive Board Assessment

Executive Directors commended the authorities for the progress made toward macroeconomic stabilization and structural reform following a decade of civil war, public sector overexpansion, and hyperinflation in the 1980s. However, Directors noted the uneven implementation of macroeconomic and structural policies in the period leading up to the presidential elections held in October 1996. They welcomed the authorities' intention to undertake a credible medium-term economic program covering the period 1998–2000, with the goal of achieving sustainability of the public finances and the external sector, structural reform, and economic growth. They supported the authorities' request for IMF support under new ESAF arrangements.

Directors stressed the importance of achieving the programmed fiscal consolidation and implementing structural reforms that increase efficiency and foster private investment. They commended the authorities for the passage of the tax reform package in May 1997 that broadened the tax base and increased the transparency of the tax system, and they encouraged further improvements in tax administration in order to strengthen budget revenues. They also emphasized the importance of the government's commitment to control current outlays, including wages and transfers, and to reduce the size of public employment further in line with the program to reform the public sector. Directors noted that the success of the program would depend on the authorities' willingness to take additional fiscal measures in the event of underperformance in the fiscal area, or as otherwise needed to meet program objectives.

Directors noted the importance of the strengthening of the financial position of the state enterprises for the success of the overall program. They stressed the need to ensure that costs are contained and revenue increased to facilitate the achievement of the fiscal program and to prepare these entities for privatization. In this regard, they emphasized that it is critical that the government carry out its commitment to adjust the tariffs of the energy and water companies both to reflect current cost increases, and to approach long-term production costs.

Directors agreed that credit policy needs to be tight to achieve program targets. They cautioned the authorities against undue reliance on central bank short-term exchange-rate indexed instruments (CENIS) and welcomed the authorities' plan to reduce the outstanding stock of these instruments. Directors stressed that the maintenance of a sound credit policy was dependent on the authorities' success in strengthening the public sector position, ceasing the banking function of the largest state bank, and avoiding directed credit to the agricultural sector.

Directors commended the authorities' decisive actions to reduce the size of state banking operations and unify reserve requirements, while extending them to all bank liabilities with the private sector. They stressed the importance, especially in the present environment of developing a sound and competitive banking system by strengthening prudential regulations and supervision, through full and timely implementation of the financial sector adjustment program to be supported by the IDA and the IDB. They also emphasized the importance of closing or privatizing the remaining state banks.

Directors stressed that the program's structural reforms are essential to increase efficiency, foster private investment, and form the basis for social consensus to underpin the program's success. They welcomed the recent enactment of a new property rights law, emphasized the importance of gaining a speedy resolution of outstanding property claims within a comprehensive judicial reform, and noted that a sustained increase in foreign direct investment will require a nondiscriminatory treatment of domestic and foreign investment. They emphasized that it is crucial that the privatization of public enterprises take place in an appropriately sequenced and transparent process within an adequate regulatory framework. Furthermore, they urged the continued reform of both the public and financial sectors to help deepen private sector activity.

Directors were encouraged by the authorities' recent steps to improve governance. They welcomed the reduction in discretionary tax exemptions resulting from the tax reform package and the broadened coverage of the budget that is included in the program.

Directors commended the government's commitment to alleviate poverty by improving education and health services, in particular in the poorest regions, and by implementing targeted social safety net programs. They strongly supported the protection of social expenditure from further expenditure cuts, and they considered appropriate the programmed increase in such expenditure as additional concessional resources become available. Directors encouraged the government to establish a mechanism to monitor social expenditure and performance, which would help to achieve specific targets in this area.

Directors noted that the crawling peg exchange system has been helpful in protecting Nicaragua's external competitiveness, as evidenced by the continued strong growth of nontraditional exports. Some Directors agreed that a gradual reduction in the rate of the crawl may become appropriate after sustained implementation of macroeconomic and structural reforms.

Directors were encouraged by the substantial progress that has been made in reducing Nicaragua's external debt and debt service. They noted, however, that Nicaragua will continue to face a difficult external position in the coming years as a result of large debt service obligations, even after full application of traditional debt relief mechanisms. They stressed that sustainable improvements in its external debt situation would require strict adherence to the program supported by the ESAF arrangements and the avoidance of nonconcessional borrowing. Directors agreed that provision of substantial concessional assistance would be needed for years to come to support Nicaragua's reform efforts. In that context, they stressed that sustained strong performance under the program will be critical in considering Nicaragua's eventual eligibility for the HIPC Initiative. Directors welcomed the authorities' decision to publish the letter of intent and the memorandum of economic and financial policies, as this would help achieve broad public support for the program, as well as enhance the transparence of government policies.

Directors emphasized the importance of improving the quality of economic statistics in several areas, and of providing them on a timely basis to the IMF.

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Nicaragua: Selected Economic Indicators

	1994	1995	1996	Est. 1997	Proj. 1998
			In percent		
Domestic economy					
Change in real GDP	3.3	4.3	4.5	5.0	4.8
Change in consumer prices (end of period)	12.4	11.1	12.1	7.3	8.0
Unemployment rate	20.7	16.2	14.8	13.9	...
			In millions of U.S. dollars		
External economy					
Exports f.o.b.	351	526	670	791	924
Imports f.o.b.	-785	-865	-1,052	-1,235	-1,357
Current account balance	-966	-658	-641	-540	-491
Capital account balance	-281	-17	108	432	492
Current account balance (in percent of GDP)	-53.0	-34.9	-32.6	-26.8	-23.2
External debt (in percent of GDP)	641.2	635.1	310.0	291.7	278.7
Financial variables					
			In percent of GDP		
Public finance					
Combined public sector savings 1/	0.5	2.6	1.7	3.7	4.3
Combined public sector overall balance (before grants) 1/	-14.4	-12.4	-15.7	-9.7	9.0
			Annual percentage change		
Money and credit					
Financial system liabilities to private sector 2/	55.7	29.8	32.4	44.4	21.3
Financial system credit to private sector	21.3	13.7	9.9	16.6	15.9

Source: Central Bank of Nicaragua; Ministry of Finance; and IMF staff estimates.

1/ Includes operational result from the central bank.

2/ Starting in 1995, this includes central bank paper (CENIS) held by the private sector.

Press Information Notice (PIN) No. 98/14
FOR IMMEDIATE RELEASE
March 9, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Norway

The IMF Executive Board on February 23, 1998 concluded the 1997 Article IV consultation[1] with Norway.

Background

Since late 1993 Norway has pursued an economic strategy designed to preserve the competitiveness of the non-oil ("mainland") economy and help ensure that the current period of rapid expansion in oil export revenues is not followed by a contraction of income and employment when oil output begins to decline in the next century. Under this strategy—often referred to as the "Solidarity Alternative"—incomes policy is used to secure moderate wage settlements while monetary policy is oriented toward stabilizing the exchange rate. Fiscal policy is used for demand management and helps to insulate the mainland economy from developments in the oil sector by reinvesting abroad a substantial part of the government's oil revenues in the State Petroleum Fund (SPF).

Since adopting these policies Norway has experienced five consecutive years of economic expansion in excess of the growth rate of potential output, with low rates of inflation. Most of the fundamentals—growth, unemployment, and the fiscal and external positions—are among the best in Europe. In 1997, mainland GDP grew by 3.9 percent, with domestic demand replacing net exports as the engine of growth. Investment was strong, particularly in the oil sector where it grew by 25 percent, reversing the decline over the 1994-96 period. Private consumption growth

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remained healthy at 3 percent, fueled by low interest rates, brisk employment growth and the healthy financial position of the household sector. Government consumption grew by 2½ percent, mainly on account of increased local authority spending.

This favorable performance, however, is being threatened by capacity shortages and rising inflationary pressures. The tightness in labor markets has led to shortages of skilled labor in the hotel, health, and construction sectors, and firms are having to advertise across Europe to procure personnel. Continued strong growth in employment is expected to lower the unemployment rate to 3¾ percent in 1998. Inflation (i.e. changes in the CPI) has risen from 0.7 percent in March 1996 to 2 percent in January 1998 and is projected to increase further to at least 2¾ percent by the end of the year. Most non-government forecasters point to risks of even higher inflation, if wage settlements rise significantly during 1998. Asset prices have also risen sharply: housing and stock prices rose by 12 percent and 32 percent respectively, in 1997, although stock prices have fallen back somewhat since the end of last year.

The 1998 budget, which was adopted in November 1997, targeted a tight fiscal stance for the fifth consecutive year. However, the magnitude of the fiscal contraction was considerably less than in each of the previous years despite the signs of overheating of the economy and the accommodative stance of monetary policy. The non-oil structural deficit is expected to decline by ¼ percent of GDP, to slightly below 4 percent of GDP, following a cumulative tightening of 5½ percent over the 1994-97 period. The state budget surplus, which is invested in the SPF, is expected to stabilize at 5.8 percent of GDP in 1998 from approximate balance in 1995. The general government surplus is expected to widen to 7.7 percent of GDP in 1998.

Under policy guidelines adopted in 1994, the primary objective of monetary policy is to stabilize the exchange rate of the krone against European currencies around the level prevailing at the time that the fixed exchange rate system was abandoned in December 1992. The Norges Bank is also expected, to the extent consistent with the goal of a stable exchange rate, to contribute to dampening fluctuations in the domestic economy. While the Norges Bank has some latitude to interpret this policy flexibly, in recent years monetary policy has generally been procyclical as interest rates were reduced to moderate a tendency toward appreciation of the exchange rate. Between October 1996 and January 1997 the Norges Bank lowered official short-term interest rates by 125 basis points. Subsequently, in July, the Norges Bank raised its official short-term interest rate by 25 basis points in response to downward pressure on the exchange rate while, in October, the Norges Bank maintained its official rate unchanged in the wake of the Bundesbank's 30 basis point interest rate hike. The Norway-German short-term interest rate differential is presently about 50 basis points, leaving Norwegian interest rates well below the EU average.

Executive Board Assessment

Executive Directors welcomed Norway's impressive economic performance, marked by five consecutive years of rapid growth, a sharp fall in unemployment, significant gains in real wages low inflation, and strong fiscal and external positions. They considered Norway's macroeconomic

strategy—the so-called Solidarity Alternative—and structural reforms to have been instrumental in these achievements.

Directors underscored, however, the fact that the authorities now faced important challenges in preserving and extending these gains. For the immediate future, the priority must be to prevent further overheating of the economy, as evidenced by the emergence of capacity constraints in a number of sectors, the gradual but continuous upturn in underlying inflation, and the sharp increases in asset prices and associated bank lending. For the longer run, the primary challenge will be to promote sustainable growth and stable financial conditions in the face of fluctuations in oil income and demographic change. In pursuing these objectives, Directors noted that Norway's macroeconomic strategy, which relies upon monetary policy to stabilize the exchange rate and incomes policy to attain moderate wage settlements, places a heavy burden on fiscal policy.

Directors considered that the marginally contractionary fiscal stance adopted in the 1998 budget was likely to be insufficient to avoid an intensification of inflationary pressures. They urged the Norwegian authorities to take additional measures as soon as possible to reduce the non-oil budget deficit further. In light of the high tax burden on the mainland economy, Directors suggested that fiscal adjustment should focus mainly on expenditure restraint, with particular emphasis on reducing subsidies, tax preferences, and public sector employment. They noted that a strengthening of fiscal policy along these lines would help safeguard the ability of the State Petroleum Fund to insulate the mainland economy from fluctuations in oil earnings—a goal the importance of which had been highlighted by the recent downturn in world oil prices—and to cover the increase in pension-related expenditures as the population ages.

Against this background, many Directors indicated that, if fiscal policy were unable to play a sufficiently restraining role in 1998, it would be important to help alleviate demand pressures through more active use of monetary policy. A key element in this judgment was the concern that the present policy mix would be unable to forestall a significant increase in wages in the face of excess demand and tight labor markets. Some Directors suggested, however, that it would be preferable for the Norwegian authorities not to deviate from the current exchange rate targeting framework, judging that there was a risk that significant appreciation of the exchange rate would undermine support for the incomes policy. In general, Directors felt that it would be desirable to preserve the transparent and consensual approach to economic policy that had contributed to the success of the Solidarity Alternative strategy. In that context, Directors considered that wage and price developments during the coming year, and the fiscal policy response, would shed important light on the sustainability of the strategy and the appropriate framework for monetary policy.

Directors welcomed recent structural measures, including those taken in the context of Norway's participation in the European Economic Area, but noted that there was a substantial agenda of unfinished business. They encouraged the authorities to reduce Norway's protection of the agricultural sector and noted that there was scope for further measures to increase labor market flexibility. Directors also supported the proposals to promote greater neutrality in the tax system.

Directors emphasized the importance of further steps to strengthen the banking system, through continued strong supervision, higher capitalization in some institutions, and further gains in bank efficiency. To that end, they encouraged the authorities to reduce legal impediments to consolidation in the banking sector and to consider phasing out more rapidly the government's remaining ownership stake in Norway's largest commercial banks.

Finally, Directors welcomed Norway's continued commitment to a high level of official development assistance.

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Norway: Selected Economic Indicators

	1994	1995	1996	1997	1998 1/
Real Economy (change in percent)					
Real GDP	5.5	3.6	5.3	3.5	4.8
Of which: Mainland GDP 2/	4.1	3.1	3.7	3.9	3.2
Domestic demand	3.8	4.3	3.7	6.2	3.1
CPI	1.4	2.5	1.3	2.6	2.8
Unemployment rate (in percent)	5.4	4.9	4.9	4.1	3.8
Gross national saving 3/	25.0	27.0	29.9	30.6	31.9
Gross domestic investment 3/	22.3	23.7	22.8	25.1	24.5
Public Finance (in percent of GDP)					
State budget balance	-3.3	0.4	4.6	5.8	5.8
General government financial balance	0.4	3.3	5.9	7.0	7.7
Money and Credit (end-period, percent change)					
M2	6.5	5.1	6.0	4.7	...
Interest rates (period average, in percent)					
Three-month interbank rate	5.8	5.5	4.9	3.7	...
Ten-year government bond yield	7.5	7.4	6.8	5.9	...
Balance of Payments (in percent of GDP)					
Trade balance	5.5	5.4	8.2	7.2	8.5
Current account	2.6	3.1	7.1	5.5	7.5
Reserves (gold valued at SDR 35 per ounce, end of period, in billions of SDRs)	13.1	15.2	18.5	17.3	...
Exchange rate					
Exchange rate regime			Managed floating		
Present rate (February 20, 1998)			US$1 = Nkr 7.57		
Nominal effective rate (1990=100)	96.7	99.22	98.9	99.4	...
Real effective rate (1990=100) 4/	98.5	104.2	106.6	108.5	...

Sources: Statistics Norway, Norges Bank, International Financial Statistics and staff estimates.

1/ Staff projections.
2/ Excluding petroleum and shipping activities.
3/ In percent of GDP.
4/ Based on relative normalized unit labor costs in manufacturing.
5/ These projections are based on the oil price assumption in the 1998 budget. If oil prices remain at their current level, about 15 percent below the assumption in the 1998 budget, the fiscal and external current account surpluses would be reduced by about 1½ percent of GDP.

Press Information Notice (PIN) No. 98/21
FOR IMMEDIATE RELEASE
March 30, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Poland

The IMF Executive Board on March 16, 1998 concluded the 1997 Article IV consultation[1] with Poland.

Background

Poland has been able to combine strong economic growth—the fastest in Eastern and Central Europe over the past four years—with substantial declines in inflation. Close to two-thirds of all jobs in the economy are now in the private sector, illustrating that the country's transition remains firmly on track. Economic activity was robust in 1997. Strong investment spending and the fastest real retail sales increases since the transition started combined to push real GDP growth to 6.9 percent for the year. Investment was driven by strong demand, growing credit availability, and, increasingly, by foreign direct investment, while rapid increases in real wages served to underpin consumer spending. In the face of this strong growth, the unemployment rate declined noticeably. Contrary to initial fears, the serious floods that damaged the country last summer apparently had relatively limited macroeconomic effects.

This strong domestic spending had a negative effect on the current account which, led by rapidly growing imports, deteriorated from a surplus of more than 3 percent of GDP in 1995 to a deficit of 3.2 percent of GDP in 1997. International competitiveness does not appear to have been a problem. An index of the real effective exchange rate (unit labor cost basis) shows little loss of competitiveness over the past year and a half, suggesting that strong domestic demand has been the dominant factor behind the current account's deterioration.

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

Inflation declined steadily in 1997. The December-to-December increase in the CPI dropped from 19 percent in 1996 to about 13 percent in 1997. Underlying this trend were healthy productivity growth, which kept unit labor costs constrained, and continued downward price pressure from imports. CPI inflation increased somewhat in January and February 1998, although PPI inflation declined.

Broad money and credit to nongovernment both registered vigorous growth in 1997. The monetary authorities tightened policy several times during 1997, both by raising reserve requirements and by increasing headline interest rates. Partly in response, the pace of expansion of money and credit showed signs of slowing down late in the year. For example, rates of increase of credit to the nongovernment sector (seasonally adjusted) fell to about 2 percent per month or less starting in October from close to 3 percent on average in the first nine months of the year. The zloty, managed via a currency basket arrangement with a ± 7 percent band with a central rate that depreciated by 1 percent a month throughout 1997, traded on the weak side of parity during the period of global financial market gyrations during the second half of the year, but appreciated sharply from January through March 1998. In late February 1998 the band was widened to ± 10 percent and the rate of crawl was reduced to 0.8 percent per month.

Assisted by a macroeconomy that exceeded official growth projections, the budget deficit of the general government was 1.8 percent of GDP in 1997—substantially below the initial target of about 3 percent of GDP, and an improved fiscal position from 1996. Contributing to the lower deficit were privatization revenues, value-added tax (VAT) revenues, and central bank transfers that were higher than expected, and cyclically sensitive expenditures—such as unemployment benefit payments—that were significantly below budget. Privatization revenues amounted to about 1½ percent of GDP. Spending on the flood emergency was largely offset by cutbacks elsewhere in the budget. Public debt declined as a percentage of GDP in 1997 for the fourth year in a row.

Favorable conditions are expected to continue in 1998, although the pace of domestic demand is expected to moderate somewhat. Slowing credit expansion is expected to cause some easing in the pace of investment spending, and more modest real wage increases will dampen consumption. Notwithstanding a slowdown in the growth of imports, the current account is expected to worsen, though at a much slower pace than in the last two years.

Executive Board Assessment

Executive Directors commended Poland for its continued record of impressive economic performance, as reflected in the achievement of sustained strong economic growth with attendant gains in living standards, combined with substantial declines in inflation. Directors also recognized the authorities' achievements in advancing structural reforms. Directors saw Poland as a leader among transition economies. Despite this strong record, however, they were concerned that the current account position had deteriorated sharply over the previous two years, and that inflation remained high, especially when compared with Poland's main trading partners. Directors remarked that real domestic demand had been increasing at unsustainable

rates over the previous two years. As this was the primary factor behind the deterioration of the current account, Directors cautioned that such rapid growth should be stemmed to prevent a further worsening of the current account and to help achieve the disinflation objectives.

Several speakers pointed out that recent developments in Asia and other parts of Central Europe had demonstrated the importance of limiting external vulnerability and the associated disruptions. While recognizing the significant reliance in Poland on nondebt-creating inflows to finance the external deficit and the comfortable reserve position, Directors nonetheless underscored the need for addressing the weakening external position with an appropriate strengthening of macroeconomic policies. Directors also highlighted the importance of such policies for achieving a further reduction in the still high inflation rate and inflationary expectations in the economy. Directors therefore agreed that the main challenges for economic policies in 1998 are to stabilize the current account and maintain the momentum of disinflation. To this end, they saw the need to accelerate fiscal consolidation, accompanied by strong wage restraint, as well as to strengthen the pace of privatization and social security and health care reforms.

Directors welcomed the actions taken by the authorities to tighten monetary policy throughout 1997, and to keep the 1997 budget deficit below the initially targeted level, as steps in the right direction. In their judgment, however, additional action was now necessary. As monetary policy was already tight, the main burden should be borne by fiscal policy. Many speakers indicated that an appropriate target would be to balance the budgetary accounts of the general government in 1999 without increased reliance on privatization revenues. As a first step, they argued that, through firm implementation of the budget, the deficit in 1998 should be kept below the formal target, as had been done in recent years, with a focus on expenditure reduction. A few Directors did not see a clear case for stronger fiscal consolidation, and attached greater importance to other policies, such as reducing private expenditure through stronger wage restraint, in the effort to reduce inflation.

Directors agreed that monetary policy would have to be conducted carefully in 1998. Directors commented that maintaining the existing tight monetary stance was appropriate until the slower pace of credit expansion was confirmed, and the stance of fiscal policy gave confidence that policies were in place to control the pace of domestic demand growth. With real interest rates expected to decline gradually later in 1998 and in 1999, the rate of increase in money demand should slow significantly. Some speakers commented that the growth of the monetary aggregates would thus need to be monitored closely to prevent an inflationary policy bias.

Directors noted that the progressive reduction in the rate of crawl of the zloty had been a driving force behind the disinflation process in Poland in the last several years. They agreed that with the rate of crawl unchanged for 24 months, it had gone from imposing a ceiling on inflation to a floor. Most Directors welcomed the recent decision of the National Bank of Poland to lower the rate of crawl of the zloty, and a few speakers saw a need for further steps in this direction. Most Directors very much welcomed the widening of the band around the zloty's central rate, as the greater flexibility of the rate would help discourage short-term capital flows and assist in the disinflation effort. Some speakers saw this as a step toward a more flexible exchange rate policy.

Directors welcomed the strengthening of the independence of the central bank, notably the primacy given to price stability as a goal of policy, and the prohibition on direct financing to the government by the central bank after October 1998. Some Directors expressed concern at the lack of staggered terms for Council members, which might undermine confidence in the continuity of policy. They suggested that this provision be revisited at an early stage.

Some Directors felt that the rapid expansion of credit during the past two years highlighted the need to strengthen bank supervision. They expressed concern about the rising bad loan ratios on installment loans, and recommended an early tightening of prudential rules.

Directors expressed concern that continued excessive wage growth could slow the momentum of disinflation, fuel demand for consumer goods, and contribute to a further worsening of the external sector. Directors urged the authorities to limit wage increases in state enterprises to the specified norm. In their view, wage increases that had consistently exceeded in recent years the limits recommended by the Tripartite Commission represented a missed opportunity to lower inflation more rapidly. Restraining the growth of real wages in the budgetary sphere to the 2 percent specified in the budget would help by providing an important demonstration effect to the private sector.

While noting the significant progress made on structural reform, Directors emphasized the importance of further efforts, both to enhance growth prospects and to achieve fiscal viability. The authorities were encouraged to accelerate the privatization process, including in the banking sector, to help improve efficiency. Many speakers stressed that, in addition to ensuring that wage increases in more sectors of the economy were in line with productivity growth, accelerating privatization would help improve corporate governance and foster the restructuring of the economy. While some Directors noted that strategic investors could play a significant role in the privatization of several sectors, they noted that this policy may not be appropriate in all areas.

Directors encouraged the authorities to press forward with pension reform, which should also help increase domestic savings, and with reform of the health care system.

Directors expressed concern about the use of payment arrears for the payment of taxes, and recommended that the use of arrears in fulfillment of tax obligations be terminated.

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Poland: Main Economic Indicators

	1993	1994	1995	1996	Est. 1997
Real economy (change in percent)					
Real GDP	3.8	5.2	7.0	6.1	6.9
Domestic demand	5.9	4.7	6.9	9.8	8.9
CPI (end-year)	37.6	29.5	21.6	18.5	13.2
Unemployment rate (in percent)	16.4	16.0	14.9	13.6	10.5
Gross national saving (percent of GDP)	15.5	18.2	21.3	19.4	19.7
Gross domestic investment (percent of GDP)	15.6	15.9	18.0	20.4	22.9
Public finance (in percent of GDP)					
General government balance	-2.9	-2.5	-2.3	-2.5	-1.8
Public debt	86.0	69.5	55.7	49.4	47.9
Money and credit (end of period, percent change)					
Net domestic assets 1/	21.7	22.5	5.3	19.8	11.7
Money and quasi-money	36.0	33.8	39.4	29.2	30.7
Lending rate (annual average in percent)	43.2	38.9	32.3	25.6	25.5
Balance of payments in convertible currencies					
Trade balance (in percent of GDP)	-2.7	-0.9	-1.5	-6.1	-8.3
Current account (in percent of GDP)					
Including unrecorded trade	-0.1	2.3	3.3	-1.0	-3.2
Gross official reserves (in billions of U.S. dollars)	4.3	6.0	15.0	18.0	20.7
Reserve cover (months of imports of GNFS)	3.0	3.6	6.5	6.0	5.9
External debt (end of period) 2/					
(In billions of U.S. dollars)	48.4	42.2	44.0	40.6	38.1
External debt service ratio 3/					
Due	21.5	16.2	12.2	7.8	5.9
Paid	12.1	10.1	12.2	7.8	5.9
Fund position (in millions of SDRs)					
Quota			988.5		
Holdings of zloty (end-December 1997)			911.4		
Holdings of SDRs (end-December 1997)			4.0		
Exchange rate					
Exchange rate regime	Crawling band 4/				
Present rate	Zl 3.46 per US$1 (Wednesday March 18)				
Depreciation (-) against U.S. dollar					
(period average, in percent)	-24.9	-20.2	-6.3	-10.1	-17.8
Depreciation (-) of real effective exchange rate					
(relative CPIs, in percent)	7.6	0.9	8.0	8.8	2.4

Sources: Central Statistical Office, Rocznik Statystyczny; data provided by the authorities; and staff estimates.

1/ In relation to broad money at end of the previous year.

2/ Including arrears and the Fund.

3/ In percent of exports of goods and nonfactor services in convertible currencies, including the Fund.

4/ Since May 16, 1995, the zloty has been allowed to float within a ± 7 percent band around the central rate, which depreciates at a fixed monthly rate (1.0 percent since January 8, 1996) against a basket of currencies.

Press Information Notice (PIN) No. 98/19
FOR IMMEDIATE RELEASE
March 16, 1998
Corrected: 3/17/98

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Singapore

The IMF Executive Board on February 20, concluded the 1998 Article IV consultation[1] with Singapore.*

Background

Singapore's economy, which is very sensitive to developments in the world electronics market, experienced a slowdown in mid-1996, mainly on account of the decline in the global demand for computers and semiconductors which dampened manufacturing output and exports. The slowdown was helpful in reducing the positive output gap that had built up during 1993-95 as a result of the near double-digit expansion posted in those years. Consumer price inflation, which had averaged about 2 percent in Singapore over the previous decade, fell to a low of 1.4 percent in 1996, and property price inflation, which had averaged 30 percent annually during 1993-95, fell to 5 percent in 1996, following measures introduced in May to curb speculative demand in the private residential housing market. The slowdown of mid-1996 proved short-lived, however, with activity picking up in the last quarter of the year and further in 1997, fueled by a rebound in the global electronics market and an easing of macroeconomic policies.

As a result, for 1997 as a whole, growth increased to nearly 8 percent while consumer price inflation picked up to 2 percent. By contrast, property prices fell 12 percent in 1997, reflecting the impact of the May 1996 measures and additional policies introduced in April 1997 aimed at the

*Corrected first sentence.

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

resale market for public housing. The external current account remained in very sizable surplus in 1997, and reserves—although falling in US$ terms in the second half of the year—remained at about 7 months' import cover at the end of the year.

At end-1997, local financial institutions had capital ratios above the mandated 12 percent level, and were fully provisioned for classified loans, which represented 2.3 percent of global assets. Aggregate loan exposure of local banks (including their overseas branches and subsidiaries) to Malaysia, Indonesia, Thailand, Korea, and the Philippines constituted 16 percent of total assets at end-1997. The proportion of classified loans among the banks' regional loans was 5.7 percent. Exposure to the local property sector was also sizable, comprising about one-third of total domestic bank lending.

With regard to fiscal policy, which has a medium-term focus in Singapore, the primary operating surplus declined from 6 percent of GDP in FY 1995/96 (April-March) to 4 percent in FY 1996/97, reflecting mainly sizable increases in development expenditures associated with a number of infrastructural projects. A further decline to about 3 percent is targeted in the FY 1997/98 budget. A number of fiscal incentives to the financial sector (especially to boost activity for Asian Currency Units and fund management) were included in the current budget.

Monetary policy, which is the principal instrument of demand management and is centered on the exchange rate, was eased in response to the economic slowdown and the benign outlook for inflation. As a result, rather than appreciating by about 3 percent a year as it has for the past decade, the nominal effective exchange rate (as calculated by the IMF) depreciated by about 1 percent during 1997. The real effective exchange rate (on a similar basis) also depreciated slightly during 1997. In response to heightened regional currency instability since July, the authorities allowed the nominal effective value of the Singapore dollar to fluctuate within a wider range.

In line with regional developments, the Singapore dollar experienced several bouts of downward pressure against the U.S. dollar since mid-1997, resulting in a cumulative bilateral depreciation of 12 percent through mid-February. Singapore's main stock market index declined by about 20 percent over the same period.

Executive Board Assessment

Executive Directors noted that, over the past 18 months, Singapore had been faced with a number of economic challenges—including the slowdown in the electronics industry, a downturn in equity and property markets, and regional financial market turbulence—and they commended the authorities for managing their economic policies successfully under difficult circumstances. They noted that Singapore's strong fundamentals—including its high saving rate, large fiscal and external current account surpluses, flexible markets, robust reserve position, and high standard of regulation and supervision for domestic financial institutions—had helped to shield its financial market from the regional turmoil and had allowed foreign investors to remain confident about Singapore's short- and medium-term prospects.

However, Directors observed that there are still downside risks associated with the regional economic slowdown, and that, even in the absence of further unexpected regional spill-overs, growth in Singapore will slow down sharply this year, and the negative output gap is expected to widen. In these circumstances, and given the strength of the external and fiscal positions, Directors saw the small reduction in the primary operating surplus envisaged for FY 1997/98 as appropriate. They suggested that, in moving toward the medium-term objective of a lower primary operating surplus, corporate and personal income tax rates should be reduced in next year's budget alongside the intended increases in development expenditure.

Directors endorsed the authorities' intention to maintain an easier monetary policy stance as long as the inflationary outlook remains subdued, but to review the stance at frequent intervals to ensure that inflation remains low. They supported the recent increase in the flexibility of exchange rate policy, given the volatility of regional currencies, although a renewed trend appreciation of the Singapore dollar would be appropriate once the regional situation stabilizes and output returns to its potential level. They considered that market-driven hikes in interest rates should not be resisted during periods of currency turmoil.

Directors noted that available indicators suggested that Singaporean banks and finance companies were sound, with high capital ratios and low levels of classified loans in relation to portfolios. However, given their exposure to the region and to the local property market, Directors noted that the financial position of Singaporean financial institutions would probably deteriorate in the near future as provisioning for classified loans increased. While the authorities remained confident that the financial system would weather the storm, Directors cautioned that timely monitoring would continue to be essential, in view of the risks of further declines in property prices and a deterioration in the quality of the regional portfolio. To enhance confidence, Directors urged that disclosure standards of individual banks be improved, including with respect to their regional exposure, capital ratios, level of nonperforming loans, and level of hidden reserves. In view of the strength of the banking sector, this would reduce the risk of unwarranted contagion.

Directors welcomed the new package of measures introduced in November 1997 to help stabilize the property and construction sectors. They encouraged the authorities to closely monitor credit growth in these sectors.

With the recent recovery in export growth, Directors were of the view that the earlier slowdown appears to have been primarily cyclical. While the depreciation of regional currencies would have some impact on Singapore's exports, this effect would be constrained by the limited extent of export market competition with the regional economies. This said, continued restructuring of the economy into higher value-added sectors and upgrading of the skill level of the workforce were essential to safeguard Singapore's competitiveness over the medium term.

Several Directors felt that further steps to ease restrictions on the internationalization of the Singapore dollar would be appropriate and in the long-term interest of Singapore as a regional financial center. They stressed that Singapore's strong fundamentals and healthy reserve position would tend to mitigate any costs associated with possibly greater volatility of capital

flows. However, some Directors, noting that the existing restrictions, backed by strong fundamentals, had helped to mitigate the impact of regional speculative pressures on Singapore, suggested that a cautious approach in eliminating the restrictions would be warranted in present circumstances. Directors welcomed the recent recommendations made by the Subcommittee on Finance and Banking of the Committee on Competitiveness aimed at securing Singapore's position as a regional financial center. They noted the positive market reaction and encouraged the authorities to follow up on these recommendations as soon as possible.

Directors called attention to the limitations in published statistics relating to the external sector—including the coverage of the trade and services accounts of the balance of payments and the absence of data on external assets and liabilities vis-à-vis nonresidents. They urged the authorities to address these promptly to enhance the analysis of external policies. With respect to public sector data, Directors urged the authorities to increase transparency regarding holdings of government assets abroad and the net open forward position of the Monetary Authority of Singapore , and to broaden the coverage and to improve the breakdown of the public sector accounts so as to facilitate economic analysis.

Directors welcomed Singapore's ongoing efforts with respect to the provision of regional technical assistance, including the recent agreement to open the IMF-Singapore Regional Training Institute in May 1998.

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Singapore: Selected Economic and Financial Indicators

	1994	1995	1996	1997 Proj.
	(Change in percent)			
Real economy				
Real GDP	10.5	8.8	7.0	7.6
Real domestic demand	3.2	8.2	10.6	12.2
CPI inflation (period average)	3.1	1.7	1.4	2.0
Unemployment rate (annual average, in percent)	2.0	2.0	2.0	1.8
Gross national savings (percent of GDP)	49.8	50.0	50.1	51.9
Gross capital formation (percent of GDP)	32.7	33.1	35.1	37.6
	(Percent of GDP)			
Public finance 1/				
Revenue and grants	33.1	33.1	35.1	38.3
Expenditure, net lending, and fund transfers	19.9	21.5	27.0	27.2
Overall surplus	13.2	11.6	8.2	11.1
Primary surplus 2/	8.6	6.1	4.0	3.6
	(Change in percent)			
Money and credit (end of period)				
Broad money (M2)	14.4	8.5	9.8	10.3
Credit to private sector 3/	15.3	20.3	15.8	13.5
Interest rate (three-month interbank, in percent)	4.4	2.4	3.4	9.0
Foreign trade				
Export volume	27.6	16.1	7.3	8.5
Import volume	14.7	13.8	7.1	9.2
	(US$ billions)			
Balance of payments				
Exports, f.o.b.	95.0	115.5	122.5	122.3
Imports, f.o.b.	-96.0	-116.8	-123.1	-124.0
Services and transfers, net	13.2	15.7	14.7	15.8
Current account balance	12.1	14.4	14.1	14.1
(In percent of GDP)	(17.1)	(16.9)	(15.0)	(14.3)
Overall balance 4/	9.9	10.5	8.2	-2.3
Gross official reserves (US$ billion)	58.3	68.8	77.0	71.3
(In months of imports) 5/	(7.3)	(7.1)	(7.5)	(6.9)
	(End of period)			
Exchange rate				
S$/US$	1.461	1.414	1.400	1.678
Nominal effective exchange rate 6/	117.6	120.5	125.9	124.5
Real effective exchange rate 6/	112.9	113.7	118.0	116.4

Sources: Data provided by the Singapore authorities; and staff estimates and projections.
1/ Fiscal year beginning April 1; in percent of estimated fiscal year GDP.
2/ Equals overall surplus excluding net lending, capital revenue, investment income, debt interest, and fund transfers.
3/ November for 1997.
4/ Includes valuation changes in official reserves.
5/ Reserves value using end-period exchange rates; imports valued using period-average exchange rates.
6/ IMF calculations, Information Notice System index (1990 = 100).

Press Information Notice (PIN) No. 98/3
FOR IMMEDIATE RELEASE
January 26, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Slovenia

The IMF Executive Board on January 9, 1998 concluded the 1997 Article IV consultation[1] with Slovenia.

Background

Aided by a favorable starting position, independent Slovenia took an early lead among Central and East European transition countries in stabilizing and transforming its economy: by 1996, inflation had been lowered to single digits, per capita income had returned to its pre-independence level, and the international reserves position had become very comfortable. After moderating from 5.3 percent in 1994 to 4.1 percent in 1995, real GDP growth slowed further to 3.1 percent in 1996. As in 1995, domestic demand was the driving force behind the expansion in 1996, but with a clear slowdown in the growth of private consumption and investment. During 1997 real GDP growth is estimated to have risen to 3.7 percent, mostly reflecting the recovery abroad. The rate of inflation has remained stuck in the 7–11 percent range since August 1995, reflecting the combined effect of nominal effective depreciation, price adjustments for petroleum products and electricity, and wage pressure.

Real wages continued to grow strongly in 1996 and early 1997 as nominal wage growth exceeded the guidelines of the social agreement between business, government, and labor. In the absence of a new social agreement for 1997, a freeze on wages of civil servants and a lower

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degree of indexation restrained wages for the rest of the year. In 1996 the (RPI based) real effective exchange rate depreciated for the first time since 1992 as a large reduction in social security contributions reduced unit labor costs and the tolar weakened in nominal effective terms. After reversing itself in the first half of 1997, real effective depreciation resumed in the second half as the U.S. dollar continued to strengthened. All real exchange rate indicators point to a relatively modest appreciation of some 5–10 percent since 1993.

A small current account surplus and large capital inflows led to a record balance of payments surplus in 1996. A strong deterioration of the current account in early 1997—in part reflecting imports that had been deferred to take advantage of customs tariff reductions—is expected to have been largely reversed by year-end as merchandise exports responded to recovery in the EU. Moreover, the exports of services, especially tourism and transport, continued to grow. With the current account in approximate balance, continued capital inflows, including official borrowing and stable inward direct investment of approximately 1 percent of GDP, are projected to have raised the reserve cover to more than 5 months of imports.

The persistent capital inflows have posed a serious dilemma for monetary policy. In an effort to reduce stubborn inflation while maintaining competitiveness, the Bank of Slovenia continued to control base money, while staving off mounting currency appreciation pressure through capital inflow restrictions and sterilized intervention. High domestic interest rates and greater selectivity on the part of banks restrained the growth of credit in 1997, thus creating some room for outright intervention. Domestic interest rates, although falling gradually, have remained high in real terms, reflecting their backward indexation, capital inflow restrictions, and lack of competition among banks.

A small surplus on general government operations was recorded in 1996, thanks to buoyant tax collections and tight expenditure control. A larger central government surplus provided the resources to finance large reductions in pension contribution rates during the year and offset the rapidly rising deficit of the pension fund. While expenditure was controlled tightly in 1997 until the budget was finally approved in December, the general government finances have come under increasing pressure, mainly reflecting 1996 wage concessions, the full-year effect of the lower pension contributions, growth in social transfers, and further customs tariff reductions in connection with the EU accession and CEFTA agreements. Notwithstanding that some spending in early 1998 will be included in the 1997 budget, tight budget execution during most of 1997 makes it likely that the overall deficit will be slightly lower than the 1.5 percent of GDP envisaged in the recently approved general government budget.

The transformation to an economy based on private ownership of the means of production continues to make progress: the private sector now accounts for more than one half of value added and employment. The privatization of socially owned enterprises is nearing completion, but privatization of state-owned enterprises has yet to begin. Following their financial rehabilitation, the privatization of the two large state banks (and that of other state assets) still awaits approval of enabling legislation. Other unapproved legislation includes banking, foreign exchange, privatization of state assets, institutional reform of public service providers, public sector accounting, civil service reform, major taxes, and the pension system.

Executive Board Assessment

Executive Directors noted that tight macroeconomic policies and basic structural reforms in the years following independence had allowed Slovenia to make rapid progress toward stabilization, resume economic growth, and to improve the prospects for early EU membership. However, recent delays in structural reforms and a weakening fiscal situation threatened to impede further progress on reducing inflation and maintaining growth. Directors therefore urged the authorities to seize the opportunity offered by the favorable external environment to reduce inflation further, to make the economy more efficient and flexible, and to enhance its growth potential. In this respect, they considered that vigorous implementation of structural reforms and the rebalancing of the policy mix toward tighter fiscal and incomes policies and away from overreliance on restrictive monetary policy were crucial. Several Directors also noted that confidence in macroeconomic policy making could be improved by better policy coordination, greater transparency of policies, and administrative and regulatory reform. A few Directors further emphasized the desirability of improving governance as it relates to economic management.

Directors viewed the emergence of a fiscal deficit in 1997 and the potential of its future widening with concern. They stressed therefore that, in line with their underlying objective of overall fiscal balance, the authorities should push for the early adoption of a balanced budget for 1998 and should adopt a credible plan to reduce the relative size of government in the economy. Directors suggested that fiscal adjustment be largely expenditure-based. Priority should be given to measures to rein in the growth of spending on wages, social transfers, and pensions. The authorities should also examine ways to deliver public services more efficiently, through contracting out and privatization, for instance. Directors broadly endorsed the authorities' tax and pension reform plans and urged the early introduction of a value-added tax at a uniform rate.

The recent adoption of an annual monetary program was welcomed as an important step toward greater transparency and accountability in monetary policy. The Bank of Slovenia should be unequivocal in its commitment to sustained disinflation as its principal objective and assume responsibility for setting the inflation objective. Directors noted that monetary policy had been complicated by heavy capital inflows induced by high domestic interest rates. They stressed the importance of early action to remove the financial market distortions that kept domestic interest at a large premium. The chief actions required were deindexation of financial contracts, increased competition between banks, disallowance of the interest rate agreement among banks, and opening up to foreign bank branching. Several Directors also were of the view that, as pressure from capital inflows subsides with the decline in interest rates, the authorities should proceed with a gradual dismantling of restrictions on inflows. A few Directors cautioned against any premature dismantling of capital restrictions, noting that this should be undertaken only after the financial sector had been strengthened.

Pointing to the tendency for the real exchange rate to appreciate in the transition process, Directors considered that some nominal appreciation seemed appropriate in the period ahead to promote disinflation. Directors cautioned the authorities about making premature commitments

about price and nominal exchange rate stability, while the transition process remained incomplete and the conditions for a successful peg had not yet been established.

Directors welcomed the recent progress on tightening incomes policy and stressed the importance of keeping a tight rein on government wages and encouraging decentralized wage bargaining and result-oriented compensation in the nongovernment sector. Underscoring the importance of structural reform for sustainable growth and disinflation, Directors urged the authorities to move quickly to reinvigorate their stalled reform process. Progress was needed on many fronts to promote deindexation and price liberalization; strengthen corporate governance; privatize remaining socially-owned enterprises and state assets; make the labor market more flexible; and develop financial markets. In this context, the authorities were urged to do their utmost to help break the backlog of reform legislation. These measures would also improve the climate for foreign direct investment.

Directors welcomed progress in strengthening banking supervision and in the financial condition of banks, but noted that further improvement in the supervision of the financial sector was needed. Directors called for the speedy introduction of a comprehensive set of financial market legislation and encouraged the government to divest itself of its share in two rehabilitated banks and foster consolidation by mergers and acquisitions.

Press Information Notices (PINs) are a new series of IMF press notices (see Press Release 97/21). PINs are issued, at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

Slovenia: Selected Economic Indicators

	1993	1994	1995	1996	Proj. 1997
			In percent		
Real Economy					
Real GDP	-2.8	5.3	4.1	3.1	3.7
Domestic demand	13.3	5.6	11.0	3.2	3.6
RPI (end of period)	22.9	18.3	8.6	8.8	9.7
Unemployment rate	14.4	14.4	13.9	13.9	14.3
Gross national saving (in percent of GDP)	20.6	24.5	23.2	24.0	24.1
Gross domestic investment (in percent of GDP)	19.3	20.6	23.2	23.4	24.0
Public Finance (percent of GDP)					
Central government balance	1.3	2.5	3.0	4.5	4.0
General government balance	0.3	-0.2	0.0	0.3	-1.5
Public debt	21.1	18.6	18.8	23.2	23.5
Money and Credit (end of year) 1/					
Real credit to the private sector	8.7	11.6	32.4	8.4	1.1
M3	63.7	42.4	27.9	21.4	22.3
Interest Rates (percent) 1/					
Nominal interbank interest rate (overnight)	38.5	28.7	12.0	13.8	10.4
Real lending rate	19-20	16-17	13-14	11-12	10.0
Real deposit rates	8-11	8-11	7-10	5-7	3.7
Balance of Payments					
Trade balance (percent of GDP)	-1.2	-2.3	-5.1	-4.7	-4.7
Current account balance (percent of GDP)	1.5	4.2	-0.1	0.2	-0.1
Banking system reserves (US$million)	1,566	2,764	3,426	4,096	4,637
Reserve cover (months of imports of GNFS)	2.6	4.0	3.8	4.6	5.2
Fund Position (percent of quota)					
Holdings of currency					137.6
Holdings of SDRs					0.27
Quota (SDR millions)					150.5
Exchange Rates					
Exchange rate regime					Managed float
Present rate (December 15, 1997)					SIT 166.67 per US$1
Nominal effective exchange rate (1993=100) 1/	100.0	87.9	88.6	79.4	75.3
Real effective exchange rate (1993=100) 1/ 2/	100.0	102.8	113.8	109.3	109.8

1/ 1997 figures are as of end-September 1997.
2/ RPI based.

Press Information Notice (PIN) No. 98/25
FOR IMMEDIATE RELEASE
April 6, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Spain

The IMF Executive Board on March 16, 1998 concluded the 1998 Article IV consultation[1] with Spain.

Background

Economic activity has been increasingly buoyant, with a strong recovery in 1997 following a modest slowdown in late 1995 and early 1996. Output, which grew by 3.4 percent in 1997, has been supported by a solid increase in exports, equipment investment, and, most recently, consumption. A favorable competitive position has stimulated export growth, while declining interest rates, rising disposable incomes, and increased consumer confidence have boosted domestic demand. These developments have been helped by auspicious conditions, but are mainly the result of economic policies aimed squarely at making Spain a founding member of the European Monetary Union.

The recovery has been accompanied by a marked decline in inflation and robust employment creation. **Inflation** fell steadily, from about 5 percent in 1994 to 2 percent in 1997, marking the attainment of nominal convergence with European partners. **Employment** grew by 2.8 percent per annum in 1995-97, reflecting the strong growth of services, a shift from public works to housing construction, and a marked increase in part-time work, following steps to facilitate these arrangements in 1994. This has resulted in a rapid decline in unemployment from its peak in 1994, although, at 20.3 percent in the fourth quarter of 1997, it has remained the highest in the EU. Unemployment continues to be concentrated in the young and unskilled population.

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The **external current account** continued its trend improvement and posted a surplus of ½ of a percent of GDP in 1997. Although imports have risen with the cyclical upswing, this has been more than compensated by the rapid expansion of exports and tourism receipts. The favorable current account performance, accompanied by capital account surpluses, led the Bank of Spain's reserves to be reconstituted to levels prevailing prior to 1992, while maintaining the exchange rate within a narrow margin of its central parity.

Fiscal consolidation has been firmly aimed at fulfilling the requirements to qualify for EMU participation from the outset. Solid policy implementation in 1996 and 1997, propitious cyclical conditions, and a falling interest bill reduced the general government deficit from 6.6 percent of GDP in 1995 to 2.6 percent in 1997. On a cyclically adjusted basis, the improvement of 1996–97 amounted to 3.3 percent of GDP. This has led to a reversal of the debt dynamics, with the debt-to-GDP ratio declining from 70 percent at end-1996 to 68.3 percent at end-1997. The adjustment strategy has been to rely on expenditure reductions, with some significant structural changes but also policies of a belt-tightening nature, including a freeze in public sector wages and significant cuts in public investment.

In line with the medium-term objectives of the convergence program, the 1998 budget envisages a deficit of 2.4 percent of GDP. The higher revenues derived from the economic upturn will allow for a reduction in the fiscal deficit and an increase in social spending on education, health, and active labor market policies. The budget also perseveres with prudent policies on wages and employment. However, if the envisaged deficit of 2.4 percent of GDP is not revised downwards, the 1998 budget will not improve Spain's structural fiscal imbalance.

After its independence in 1994 and adoption of an inflation-targeting framework in 1995, the Bank of Spain geared **monetary policy** to the attainment of price convergence with core European countries by 1997. The bank met its objective fully. It pursued a tight monetary policy at the beginning and, once inflation was on a declining trend and there were no threats to the stability of the peseta in the ERM, it reduced its intervention rate cautiously. In the 12 months up to May 1997, the bank successively cut the reference 10-day repurchase rate by about 2 percentage points. Subsequently, the easing in monetary conditions came through dollar and sterling appreciation, but following the presentation of the 1998 budget to parliament, the Bank of Spain resumed cuts in the repurchase rate. It narrowed the repo differential vis-à-vis Germany to 120 basis points, while the peseta remained somewhat above its central parity. Bond yields continued their downward trend and fell by 160 basis points during the past year, bringing the long-term differential vis-à-vis German rates to historic lows now below 20 basis points.

The most significant recent advances in the **structural agenda** have been an ambitious privatization program, which yielded revenues of 2 percent of GDP in 1997, and a labor market reform that broadened the definition of fair dismissals and introduced a new type of labor contract with lower dismissal costs. In the first six months of application of the reform, the number of permanent contracts signed amounted to 480,000 (of which 330,000 were of the new type), compared with 160,000 over the same period in 1996.

Executive Board Assessment

Directors commended the authorities for the pursuit of sound macroeconomic policies that had brought Spain to the threshold of EMU. These policies had contributed to strong and broadly-based growth, full convergence of inflation to European averages, a decline in unemployment, a strong external position, and a significant narrowing of interest rate differentials vis-à-vis Germany. Against the backdrop of continued favorable growth prospects for 1998, Directors observed that the key challenge facing the authorities was to preserve and extend the recent economic gains, and particularly to sustain the high rate at which the economy created jobs in 1996–97. They encouraged the authorities to strengthen the pace of structural reform, given that in monetary union the labor and product markets would have a major shock-absorber role.

Directors complimented the Bank of Spain on its conduct of monetary policy, noting that the inflation-targeting framework that the bank had followed while keeping a close eye on the exchange rate had contributed to reducing inflation and long-term interest rates, and had helped lay the basis for the upturn in domestic demand. While recognizing that the scope for an independent monetary policy was waning rapidly, Directors suggested that the Bank of Spain be cautious regarding the reduction in official interest rates. This would lessen inflationary risks, yet still be consistent with a gradual and orderly convergence of the peseta to the rate at which it would be locked into the euro. A few Directors questioned whether, in light of the convergence of long-term interest rates, a lowering of short-term rates would have a significant impact on the economy.

Directors praised the firm implementation of fiscal policy in 1997. Most Directors noted, however, that although recent price and wage indicators augured well for meeting the inflation target in 1998, risks of wage pressures remained over a longer horizon. Thus, they stressed the need for fiscal policy to provide some restraint in the current economic upswing, thereby helping maintain Spain's very favorable competitive position. From that standpoint, and also to reduce the debt-to-GDP ratio, continuing the pace of fiscal consolidation was both desirable and feasible, beginning already in 1998. Accordingly, Directors welcomed the authorities' commitment to devote additional cyclical revenues to reducing the deficit, and a few speakers called for a downward revision in the deficit target of 2.4 percent of GDP. Beyond 1998, Directors viewed fiscal balance as the appropriate medium-term fiscal target for Spain, and some Directors believed that achieving that objective by 2000 would be appropriate.

On the structural side, Directors commended the authorities for their rapid privatization program, and welcomed the measures enacted to improve expenditure control. In their view, continued success in the latter sphere was closely linked to the observance of budgetary targets by regional governments; accordingly, the political agreement between the central government and the regions needed to be strengthened by establishing mechanisms to enforce it. Directors emphasized the importance of reforms to health care policy, public administration, and, over the longer term, pensions. On health care, some speakers advised undertaking a comprehensive cost containment policy that went beyond current efforts on drug expenditures.

Directors welcomed the government's intention to introduce a tax reform to reduce personal income tax rates and improve the efficiency of the tax. They advised the government to begin the implementation of the reform in a revenue-neutral manner, by postponing a reduction in revenues until expenditure cuts had made the reduction in taxes compatible with a balanced budget in the medium term.

There was consensus that reducing unemployment was Spain's most pressing policy challenge. In this regard, Directors considered that the labor market reform of May 1997 was an important step toward reducing dismissal costs, and thus increasing employment. They were pleased by early indications that permanent employment contracts were rising as a proportion of the total, and welcomed the improved industrial relations climate since the reform. They noted, however, that dismissal costs remained much higher in Spain than in other European countries. Directors therefore encouraged the authorities to persevere with reforms to reduce dismissal costs further, and to extend the policy effort to other areas where rigidities remained, such as the wage bargaining scheme and the system that superimposed unemployment benefits and dismissal payments. Directors also called for an improvement in labor statistics.

To maintain Spain's favorable competitive position at the start of EMU, Directors stressed the importance of complementing wage moderation with efficiency-enhancing structural reforms, including measures in the areas of retail trade, availability of land for urbanization, and full liberalization of the rental market.

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Spain: Selected Economic Indicators

	1994	1995	1996	1997	1998 1/
Real economy (change in percent)					
GDP	2.2	2.7	2.3	3.4	3.4
Domestic demand	1.3	3.2	1.4	2.7	3.9
CPI (end period)	4.3	4.3	3.2	2.0	2.3
Employment	-0.9	2.7	2.9	3.0	2.5
Unemployment (in percent)	24.2	22.9	22.2	20.8	19.7
Investment 2/	20.0	21.1	20.6	20.5	21.3
Savings 2/	18.6	21.3	20.9	21.0	21.6
Public finance (in percent of GDP)					
Central goverment balance	-5.1	-5.5	-3.4	-2.1	-1.9
General government balance 3/	-6.3	-6.6	-4.4	-2.6	-2.4
General government debt 3/	62.6	65.3	69.8	68.3	66.9
Money (end-year, percent change)					
Broad money (ALP)	8.2	9.2	6.5	3.6	...
Interest rates (year average)					
Three-month interbank rate	7.9	8.9	7.5	5.4	...
Ten-year government bond rate	10.0	11.3	8.7	6.4	...
Balance of payments (in percent of GDP)					
Trade balance	-3.0	-3.1	-2.6	-2.5	-2.9
Current account balance	-1.4	0.2	0.3	0.5	0.3
Reserves (US$ billions)	44.5	38.2	61.8	72.5	...
Fund position (SDR billions, December 31, 1997)					
Holdings of currency				0.5	
Holdings of SDRs				0.4	
Quota				1.9	
Exchange rates					
Exchange rate regime	member of the European monetary system				
Present rate	Ptas 155.2 to US$1				
Nominal effective rate (1990=100)	80.8	80.3	80.9	77.2	...
Real effective rate (1990=100)	86.3	87.5	89.3	85.2	...

Sources: Data provided by the Spanish authorities; and IMF staff estimates.

1/ IMF staff projections,.

2/ In percent of GDP.

3/ Maastricht basis.

Press Information Notice (PIN) No. 98/29
FOR IMMEDIATE RELEASE
April 13, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Sudan

The IMF Executive Board on February 27, 1998, concluded the Article IV consultation[1] with Sudan.

Background

In February 1997, Sudan reached agreement with IMF staff on an adjustment program for the period March–December 1997 to be monitored by the staff, which aimed at: reducing the inflation rate; reducing the external current account and fiscal deficits; making significant progress toward exchange rate unification; and initiating reforms in the areas of taxation, monetary operations and exchange and trade systems.

The tightening and rebalancing of fiscal, monetary, and external policies during 1997 led to marked progress in macroeconomic stabilization. Real GDP growth is estimated to have reached 5.5 percent in 1997, while the inflation rate declined at end-1997 to 32 percent and further to 23 percent at end-February 1998 down sharply from 114 percent at end-1996. The free market exchange rate remained broadly stable during 1997, and adjustments to the official rate reduced the spread with the market rate from 23 percent at end-1996 to 6.7 percent at end-1997. While the balance of payments was somewhat weaker than in 1996 owing to a deterioration in the terms of trade, net foreign assets of the Bank of Sudan improved due to payments to the IMF and accumulation of arrears to other external creditors. Sudan paid SDR 43.8 million to the IMF, which reduced its arrears to the IMF by SDR 16 million.

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The overall fiscal deficit was reduced sharply from 3.4 percent of GDP in 1996 to 0.8 percent of GDP in 1997, through revenue efforts (0.6 percent of GDP) and substantial expenditure restraint (2 percent of GDP). The improved revenue performance over the previous year reflected measures adopted in early 1997, including the application of the official dealer exchange rate for customs valuation (rather than the more appreciated customs exchange rate), realistic pricing policies for petroleum products after elimination of subsidies, curtailment of tax exemptions, and improved tax administration. The strong fiscal adjustment allowed for a substantial reduction of government borrowing from the Bank of Sudan, which declined to 0.5 percent of GDP from 3.2 percent of GDP in 1996, contributing to a rapid deceleration in monetary expansion to 37 percent (compared with 65 percent in the preceding year). Furthermore, increases in the Bank of Sudan cost of borrowing reference rates led to a substantial rise in real lending rates and real rates of return on deposits for investment purposes reached positive levels in 1997, following several years of substantially negative rates.

In addition, substantial progress has been achieved in the design and initial implementation of structural reforms in the fiscal, monetary, and exchange system areas. Preparations for the reform of the indirect tax system were completed and preparatory steps for the introduction of the value-added tax (VAT) were initiated. Progress was also made in improving budget management and monitoring. Important reforms were implemented to improve the quality of banking supervision, including through strengthening internal controls in banks, and initiating accounting reforms with a view to standardizing banks' financial statements. Non-debt instruments of market-based monetary management, consistent with Islamic banking principles, were developed and are expected to be used in the conduct of monetary policy during 1998. Also, measures were taken in 1997 to improve the efficiency of the foreign exchange market and to prepare for a phasing-in of a transparent, unified, and market-based exchange regime including the reduction of export surrender requirements to the Bank of Sudan and an increased role for the private sector in imports of petroleum products.

The government has formulated a medium-term reform program covering 1998–2003 which aims at achieving an average real GDP growth of 6 percent a year, reducing inflation to 5 percent by 2000, and improving Sudan's external accounts, by addressing long-standing structural rigidities, mobilizing private savings, and encouraging foreign direct investment. Consistent with these goals, the authorities have adopted for 1998 a strengthened adjustment program, that is being monitored by the staff and the Executive Board will review the implementation of the program on a quarterly basis. The 1998 staff-monitored program targets a real GDP growth rate of 6.5 percent, end-year inflation of 15 percent, and an improvement in the overall balance of payments. The program calls for containing central bank financing to the government to 0.3 percent of GDP and a significant tightening of credit expansion, consistent with the inflation target. Macroeconomic policies will be complemented by structural reforms in the areas of taxation (reform of the indirect and direct tax systems, including preparations for the introduction of the VAT), budget management (expenditure controls and monitoring), the

monetary and banking sector (introduction of new monetary instruments), the exchange and trade system (unification of exchange markets and tariff reform), privatization, the investment regime, and the agriculture sector.

Executive Board Assessment
Executive Directors noted that performance in 1997 was satisfactory, with real economic growth, inflation, fiscal and external sector performance in line with, or exceeding, initial expectations. Important structural reforms were initiated—particularly in the monetary, exchange, and fiscal areas—laying the institutional ground for strengthening reform efforts over the medium term. Directors noted that these accomplishments had been achieved under difficult internal and external environments, including a sharp worsening of the terms of trade.

Directors welcomed the authorities' commitment to deepen economic reforms in 1998 under a program that would continue to be monitored by the staff. They were of the view that firm implementation of the program would be important to lay the foundation for sustained economic growth and moving toward normalizing financial relations with external creditors. Directors observed that the performance in 1997 and the ambitious 1998 program marked a clear departure from past reform attempts, which should help build confidence on the part of market participants and the international community. Directors encouraged the authorities to persevere with the design and implementation of urgently needed structural reforms to ensure the attainment of the ambitious medium-term goals and to improve Sudan's capacity to meet its existing financial obligations. Directors stressed that sustained implementation, a broadening and expansion of the 1998 program, efforts to increase repayments to the IMF, and progress toward regularizing relations with other creditors were elements that could provide the basis for closer cooperation with the IMF in the medium term.

Directors were encouraged by the authorities' fiscal strategy, which emphasized revenue mobilization to reduce the fiscal deficit while allowing for substantially higher development outlays. They noted that Sudan's revenue-GDP ratio remained very low, and they welcomed the authorities' plan under the 1998 staff-monitored program to broaden the tax base and improve the elasticity of the tax system. Moreover, they indicated that sustaining the pace of revenue mobilization over the medium term would depend critically on expeditious introduction of the value-added tax (VAT). On this basis, Directors urged the authorities to adhere strictly to a timetable of measures that would ensure early and effective implementation of the VAT; rationalize the indirect tax system; undertake reform of the direct tax system; and continue to curb tax exemptions. On the expenditure side, they encouraged the authorities to put more emphasis on increasing spending on social and development programs and away from unproductive expenditures, given Sudan's social and infrastructural needs and the fact that the former expenditures had reached record low levels in recent years. Directors also encouraged the authorities in their efforts to improve budgetary management.

Directors supported the authorities' intention to maintain a tight credit policy through strict limits on central bank financing of the budget deficit. The tight credit policy stance and improved monetary management instruments would permit the authorities to address the significant challenges facing them in 1998. Directors welcomed the authorities' efforts to improve the health of the banking system, including through enforcement of prudential regulations, introduction of a new accounting system, and strengthening of the banking supervisory capability of the Bank of Sudan.

Directors welcomed the authorities' plan to unify the exchange markets under a market-determined exchange rate regime by mid-1998, and underscored the importance of accelerating the monetary and exchange system reforms in support of the exchange rate unification. They urged the authorities to continue to accelerate the pace of convergence of the official exchange rate toward the free market rate, reduce the surrender requirements in the first half of 1998, and eliminate the remaining requirements in the second half of 1998. Directors emphasized the importance of removing any barriers to exports. Directors noted that, notwithstanding the planned tariff reforms in 1998, Sudan's tariff barriers remained high, and urged the authorities to undertake further tariff reforms and to remove barriers to exports.

Directors also strongly encouraged the authorities to broaden the implementation of structural reforms in other areas, including the investment regime, agricultural policies, privatization, public investment policy, and the financial sector in order to sustain economic stabilization and strengthen growth prospects.

Directors noted that Sudan had made scheduled payments to the IMF in 1997, and took note of the authorities' commitment to further reduce arrears to the IMF in 1998 by SDR 15.6 million. They urged the authorities to accelerate payments to the IMF as balance of payments developments permitted, so as to enhance Sudan's credibility and reduce the burden of its overdue obligations on IMF members.

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Sudan: Selected Economic Indicators

	1995	1996	1997 1/
		In percent	
Domestic Economy			
Change in real GDP	4.4	4.7	5.5
Change in consumer prices (end of period)	71.0	114.0	32.0
		In millions of U.S. dollars	
External economy			
Exports, f.o.b.	556	620	580
Imports, f.o.b.	-1,219	-1,547	-1,555
Current account balance (accrual basis)	-1,479	-1,848	-1,992
Capital account balance (including errors and omissions and other private capital flows	368	670	712
Overall balance (cash basis, excluding arrears)	23	13	23
		In percent of GDP 2/	
Current account balance (accrual basis)	-20.8	-24.4	-24.4
Non-interest current account	-8.6	-11.8	-10.8
Change in real effective exchange rate (in percent) 3/	-24.2	14.5	5.5
		In percent of GDP 2/	
Financial variables			
Central government balance (accrual basis)	-15.2	-20.5	-11.3
Central government balance (cash basis)	-3.2	-3.4	-0.8
Change in broad money			
(In percent of beginning broad money stock)	74.2	65.2	37.0

1/ IMF staff estimates.
2/ Unless otherwise noted.
3/ (+) = appreciation.

Press Information Notice (PIN) No. 98/13
FOR IMMEDIATE RELEASE
March 6, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Switzerland

The IMF Executive Board on February 20, 1998, concluded the 1997 Article IV consultation[1] with Switzerland.

Background

Economic activity has stagnated since 1990, owing to cyclical and structural factors. In 1997, an export-led recovery was sparked by the significant real effective depreciation of the Swiss franc from end-1995 through early-1997 and a pick up in foreign demand, particularly in continental Europe. The contribution from the net foreign balance is estimated to amount to ¼ percentage point of GDP—the first positive contribution in three years. Domestic demand remained subdued mainly due to the prolonged slump in the construction sector, while private consumption revived and investment in machinery and equipment gathered strength. The current account surplus has remained large by historical standards, reaching about 7¾ percent of GDP in 1997.

The unemployment rate has risen sharply from ½ percent in 1990 to 5¼ percent in 1997. Around three quarters of this increase was due to a rise in the structural unemployment rate to an estimated 3½ percent in 1997 which still represents one of the lowest structural rates among advanced economies. Reflecting the slack in labor markets, nominal wage growth slowed below 1 percent in 1997. CPI inflation also abated further during 1997, declining to an annual rate of 0.5 percent, the lowest CPI inflation rate since 1960 as well as the lowest rate among industrial countries in 1997.

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[1]Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

Following an extended period of fiscal retrenchment during 1993-96, fiscal policy adopted a moderately expansionary stance in 1997. The fiscal impulse was equivalent to about ¼ percentage point of GDP. The general government deficit is estimated to have widened by nearly 1 percentage point of GDP to 2¾ percent in 1997. Gross public debt is likely to rise to almost 51 percent of GDP in 1997 compared to only 31 percent in 1990. Looking ahead, the deficit of the general government in 1998 was projected to increase by nearly 1 percentage point of GDP to 3½ percent of GDP, likely one of the largest general government deficits among industrial countries in 1998. The fiscal impulse would increase to ½ percentage point of GDP. Spending would be boosted by a stimulus package adopted in May 1997. This package provided an investment subsidy by the Confederation to finance public investment projects by the cantons and communes during 1997-99, with the largest share of spending taking place in 1998.

Amid rising concerns about deteriorating external competitiveness and a prolonged slump in the real economy, monetary policy turned expansionary in 1995. The growth rate for base money growth increased sharply. By end-1997, the level of the monetary base was about 3½ percent above its medium-term target path, although unexpected demand shifts diminished the reliability of this indicator. The effective real exchange rate depreciated markedly from end-1995 through the first quarter of 1997, but it strengthened again during the remainder of 1997, particularly against the deutsche mark, in part due to "safe haven" effects related to the financial crisis in Asia. Short-term interest rates remained close to 1½ percent throughout 1997, while long-term bond yields fell during 1997 by almost 100 basis points to about 3 percent at end-1997. In its announcement of monetary policy intentions for 1998, the Swiss National Bank (SNB) envisaged a broadly unchanged monetary stance. In view of the recent instability in the demand for base money, the SNB announced that it would resort increasingly to other indicators including M3 growth to assess monetary conditions.

Average real GDP growth in Switzerland since the mid-1970s has lagged substantially behind the growth rates recorded in most other advanced economies. To reinvigorate this mediocre long-rung growth performance, the authorities have already undertaken significant structural reforms to strengthen competition in domestic markets for goods and services and to improve the functioning of the labor market.

As regards the outlook, real GDP is projected to increase by 1¾ percent in 1998 and 2 percent in 1999. Notwithstanding its current upward momentum, export growth is projected to slow as foreign demand slackens owing to developments in Asia. Domestic demand is envisaged to recover gradually during 1998-99, reflecting improved consumer sentiment, increased investment in machinery and equipment as capacity utilization rises in industry, and the end of the prolonged slump in construction. Only limited improvement is expected in the labor market, reflecting ongoing restructuring efforts in manufacturing and some service sectors including banking. Inflation is projected to be well contained by a large output gap and rising competitive pressures due to structural reforms.

Executive Board Assessment

After a prolonged period of stagnation, Directors welcomed the recovery that began in 1997 that had been sparked by a significant real effective depreciation, increased foreign demand, and supportive macroeconomic policies. They held the view that the key policy issue facing the authorities was how to nurture the nascent recovery and turn it into a sustained and vigorous expansion, while keeping inflation low. At the same time, they underscored the need to address structural rigidities in product and labor markets in order to secure a lasting return to more robust growth. Given the sizeable slack in the economy, the risks relating to developments in Asia, and possible appreciation pressures on the Swiss franc due to "safe haven" effects, most Directors considered the somewhat expansionary tilt of macroeconomic policies envisaged in 1998 as appropriate. Directors went on to note that, as the current upswing gained momentum, macroeconomic policies would need to shift carefully and progressively toward restraint. They saw this policy transition as a major challenge, given the long transmission lags of monetary policy and the institutional obstacles to conducting an effective countercyclical fiscal policy. In light of these considerations, which limited somewhat the flexibility of macroeconomic policies, several Directors attached particular importance to strong structural policies in reinvigorating the Swiss economy.

With the economy expected to gain further momentum, Directors underscored that fiscal consolidation should become the order of the day in 1999 so as to begin to reverse the recent surge in the debt-GDP ratio and to prepare for the prospective demographic pressures. In this connection, they endorsed the authorities' medium-term fiscal targets, specifically to balance the Confederation's budget by 2001 and to maintain a broadly balanced budget over the business cycle thereafter. Toward these ends, Directors emphasized the importance of making a significant step toward fiscal consolidation in 1999, and they therefore welcomed the recently proposed fiscal package. Directors also called for additional efforts aimed at improving the tax system with a view to shortening income tax collection lags, a measure promising to enhance both revenues and the operation of automatic fiscal stabilizers. In this regard, several Directors also saw room for an improved fiscal policy coordination between the various levels of government.

Directors noted that the past three years had seen an easing of monetary conditions, which was all the more welcome for not having ignited inflationary pressures. They recognized, however, the considerable uncertainty regarding the magnitude of the monetary impulse presently in the pipeline stemming from the instability in the demand for base money in recent years. Directors supported, therefore, the intention of the Swiss National Bank (SNB) to monitor more closely the trends in other monetary aggregates, in particular M3, and encouraged the SNB to monitor a broad range of other indicators, including the exchange rate, the yield curve, indicators of economic slack, and the momentum of domestic demand. However, a few Directors pointed to the sometimes conflicting signals from too broad a range of indicators. Given Switzerland's weaker cyclical position compared with the rest of Europe, Directors considered a relatively less rapid firming of monetary conditions appropriate, but underscored the need for continued attention to signs of emerging price pressures.

Directors welcomed the authorities' plan to reform Switzerland's monetary constitution by severing formally the link of the Swiss franc to gold, by recognizing the de facto independence of the SNB, and by clearly establishing price stability as a primary objective of the monetary authorities. These proposed changes would bring the constitutional law in line with longstanding monetary realities inside and outside of Switzerland.

Observing that for some two decades structural rigidities, particularly in the sheltered product markets, had acted as a drag on Switzerland's growth performance, Directors welcomed recent reforms to enhance domestic competition, and emphasized that their strict enforcement would be crucial to reap the intended benefits. Directors also saw a clear need for further measures to allow a greater play of market forces, and supported the slated deregulation of the communications, transport, and energy sectors.

Directors noted the increase in unemployment; particularly, long-term unemployment. While welcoming the recent adoption of active labor market policies designed to avoid the adverse effects of prolonged passive income support, Directors noted that further steps were necessary to improve convincingly the functioning of labor markets. They mentioned the need to limit the duration and generosity of unemployment benefits and to strengthen the link between unemployment contributions and benefits. While taking note of Switzerland's generally liberal trade policies, Directors regretted the slow pace of liberalization of the overly protective agricultural regime.

In the area of banking reform, Directors welcomed the progress in recent years, including the passage of the new money laundering law, and looked forward to the implementation of the amendment to the federal banking law that would help level the competitive playing field with cantonal banks. More generally, several Directors held the view that further progress in structural reform and deregulation was also justified in light of the growing proximity of EMU and the close ties of Switzerland with its European neighbors.

Directors noted that weaknesses in macroeconomic statistics hampered economic analysis and impeded the conduct of effective economic management. They called on the authorities to remedy the situation expeditiously, including through the provision of adequate budgetary resources.

Directors expressed disappointment over the further decline in official development assistance relative to GDP in 1997, and urged the authorities to increase official development assistance to at least their own official targets.

Press Information Notices (PINs) are issued at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

Switzerland: Selected Economic Indicators

	1993	1994	1995	1996	1997 1/
	(Change in percent, unless otherwise noted)				
Real economy					
Real GDP	-0.5	0.5	0.8	-0.2	0.5
Real domestic demand	-1.0	2.5	2.3	-0.2	0.3
CPI (year average)	3.3	0.9	1.8	0.8	0.5
Unemployment rate (in percent of labor force)	4.5	4.7	4.2	4.7	5.2
Gross national saving (percent of GDP)	28.9	27.7	28.5	27.2	27.1
Gross national investment (percent of GDP)	20.7	21.0	21.5	19.9	19.4
Public finances	(In percent of GDP)				
Confederation budget balance	-2.6	-1.9	-1.2	-1.5	-1.6
General government balance 2/	-3.6	-2.8	-1.8	-1.7	-2.7
Gross public debt	42.3	45.0	46.7	49.2	50.9
Balance of payments					
Trade balance	0.7	0.6	0.3	0.3	0.1
Current account	8.2	6.7	6.9	7.3	7.7
Official reserves (US$ billion) 3/ 4/	32.6	34.7	36.4	38.4	35.1
Money and interest rates	(Change in percent, unless otherwise noted)				
Monetary base (end of year) 5/	2.4	0.4	1.4	5.2	3.1
M3 (end of year) 6/	6.7	3.7	3.1	6.8	3.8
Three-month euro rate (in percent) 5/	4.8	4.0	3.0	1.9	1.6
Government bond yield (in percent) 5/	4.6	5.0	4.8	4.2	3.5
Exchange rate					
Exchange rate regime	Managed float				
Present rate (January 29, 1998)	Sw F 1.46 per US$				
Nominal effective exchange rate (1990=100)	99.8	106.3	113.3	111.6	104.2
Real effective exchange rate (1990=100) 7/	100.6	105.3	112.0	108.4	100.2

1/ IMFstaff projections, unless otherwise noted.
2/ Including Confederation, cantons, communes, and social security.
3/ Excluding gold.
4/ For 1997, average January-November 1997.
5/ For 1997, average January-November 1997.
6/ For 1997, average January-October 1997.
7/ Based on consumer prices.

Press Information Notice (PIN) No. 98/7
FOR IMMEDIATE RELEASE
February 19, 1998

International Monetary Fund
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Togo

The IMF Executive Board on Wednesday, January 21, 1998, concluded the 1997 Article IV consultation[1] with Togo.

Background

Following the devaluation of the CFA franc in January 1994, Togo adopted a comprehensive adjustment strategy supported by the IMF under a three–year arrangement under the Enhanced Structural Adjustment Facility (ESAF), aimed at achieving sustained economic growth and financial viability over the medium term. The macroeconomic and structural policies implemented by Togo under the program have led to significant improvements in a number of areas, including per capita GDP growth, the decline in inflation, and the reduction of internal and external imbalances.

Following large increases in 1995 and 1996, Togo's economic growth for 1997 is estimated at 4.8 percent. This reflects higher phosphate production and cash crop output, and some strengthening of secondary sector activity, although manufacturing activity is still affected by weak domestic demand and low levels of capacity utilization, and growth in the tertiary sector has been modest. There was a surge in transportation prices at the beginning of the year, owing to the increase in the VAT rate and higher petroleum product prices, and food prices also rose, reflecting supply constraints. As a result, annual inflation was just over 7 percent, compared with 4.9 percent in 1996.

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The government's overall deficit (on a payment order basis and excluding grants) narrowed from 6.3 percent of GDP in 1996 to 3.6 percent in 1997, reflecting efforts to rationalize the tax system and broaden the tax base, improve the tax and customs administration, and strengthen budgetary and treasury operations. The government's external debt burden declined from about 100 percent of GDP in 1996 to 94 percent in 1997, but still remains relatively high. The government also initiated a comprehensive restructuring of its domestic debt, repaying a substantial amount of domestic arrears in cash, and settled all its external payments arrears. The authorities aim to further improve the fiscal situation in the coming year, while pursuing civil service employment rationalization and domestic debt restructuring.

Broad money rose by 15.5 percent in 1997, reflecting a sharp rise in money in circulation linked to the expansion of agricultural production. Credit to the private sector picked up in the last quarter of the year, while net bank credit to the government was held to the program limits. The net foreign assets of the banking system increased by CFAF 15 billion, reflecting the improved external trade balance and inflows of proceeds from privatization. Togolese commercial banks continued their efforts to strengthen their balance sheets and substantially reduced their recourse to refinancing from the central bank. However, banks still carry a substantial amount of nonperforming loans, and their compliance with the prudential ratios set by the regional banking commission failed to improve significantly during the year. A financial sector restructuring program with the World Bank is expected to be launched in the first half of 1998.

The external current account deficit (excluding official transfers)narrowed from 6.2 percent of GDP in 1996 to 5.3 percent in 1997. The improvement stemmed from a considerable strengthening of export earnings in 1996-97, in particular in agricultural exports, which benefitted from favorable exchange rate developments and world market prices for the main commodity exports.

Prospects for 1998

Real GDP growth is projected at 5.2 percent in 1998, as phosphate production increases and the output of cash crops, particularly cotton, strengthens. After the exceptional surge in 1997, end–year inflation is expected to subside to 3.7 percent, while the external current account deficit (excluding official transfers) is projected to be roughly stable at 5.2 percent of GDP. The primary fiscal surplus is projected to increase from 0.8 percent of GDP in 1997 to 1.5 percent in 1998, reflecting the ongoing efforts to improve tax collection and to contain nonpriority outlays, while the overall fiscal deficit (excluding official transfers) is expected to widen from 3.6 percent of GDP in 1997 to 4 percent in 1998.

Executive Board Assessment

Executive Directors noted the continued recovery of economic activity in Togo, the encouraging developments in the balance of payments, and the progress made in improving the public finances and in reestablishing the momentum of structural reforms. Directors welcomed the improved performance under the program supported by the third annual arrangement under the ESAF, particularly after the slippages that had occurred in 1996. They noted the observance of

most of the quantitative and structural performance criteria and benchmarks under the program including the regularization of Togo's relations with its external creditors.

Nevertheless, Directors noted that the economy is still vulnerable to climatic and other external shocks, while macroeconomic management needs to be strengthened and structural weaknesses need to be addressed. They, therefore, urged the authorities to continue to persevere in their reform efforts aimed at promoting savings and investment, especially by the private sector, and accelerating economic diversification. Such measures would lay the basis for high quality growth and poverty alleviation, and help improve donor confidence.

While welcoming the progress made in improving the public finances, Directors observed that the overall fiscal position remains fragile and called for further fiscal consolidation. On the revenue side, they noted the strengthening of revenue collections in the second half of 1997, after the shortfalls incurred in the first few months of the year. They encouraged the authorities to continue their efforts to enhance revenue collection. Moreover, they urged the authorities to pursue vigourously the measures necessary to broaden the tax base and to reduce tax exemptions. They also stressed the need to proceed with plans to reduce the statistical tax on imports ahead of the regional schedule set for the introduction of the common external tariff. On the expenditure side, Directors emphasized that a marked improvement in expenditure control and treasury procedures was essential to ensure effective management of the cash-flow situation and to avoid any recurrence of domestic or external payments arrears. They also encouraged the authorities to integrate all financial activities of the government into the general budget and to proceed apace with the implementation of the civil service employment strategy. They also encouraged the authorities to reorient expenditures to meet social needs.

Directors welcomed the implementation of the domestic debt restructuring plan and the substantial repayments of domestic arrears, underscoring their importance for strengthening the financial situation of public and private enterprises. They urged the authorities to continue the repayment of domestic arrears during 1998.

Directors were disappointed by the slow progress toward full compliance of banks operating in Togo with the established prudential norms, and expressed concern about the significant level of nonperforming loans. They urged the authorities to cooperate closely with the regional banking commission to strengthen the position of weak banks, to reduce government involvement in the banking sector and privatize state-owned banks, and to reform the legal environment for banking operations in order to facilitate loan recovery.

Directors noted the efforts of the authorities to reestablish the momentum of structural reforms following the slippages of 1996, particularly in the areas of public enterprise reform and privatization. They encouraged the authorities to proceed expeditiously with the new phase of the privatization program, and to complete soon the sale of part of the government's shares in the phosphate company. Directors also stressed the importance of prompt implementation of the planned reforms of the legal and regulatory framework for economic activity, particularly the envisaged strengthening of the judiciary. These reforms would help to create a more propitious environment for private saving and investment. In this context, they encouraged the authorities

to press ahead with the regional integration initiatives that were under way, and to ensure that the regulatory framework would encourage private capital flows.

Directors stressed the need to improve further the availability, quality, and timeliness of Togo's core economic and financial data, particularly as regards the monetary and balance of payments data, and to take prompt action to strengthen the statistical apparatus.

Press Information Notices (PINs) are a new series of IMF press notices (see Press Release 97/21). PINs are issued, at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

Togo: Selected Economic Indicators

	1993	1994	1995	1996	1997 1/
			Annual percentage change		
Domestic economy					
Change in real GDP	-16.4	16.8	6.8	8.2	4.8
GDP deflator	-6.8	33.6	12.7	5.2	5.4
Change in consumer prices (end of period)	2.4	48.5	6.4	4.9	7.2
			In percent of GDP 2/		
Gross fixed investment	7.6	15.1	16.1	16.3	15.2
Gross domestic savings	-0.1	11.4	11.9	11.4	11.2
Gross national savings	1.1	9.3	12.0	12.3	13.1
			In millions of U.S. dollars 2/		
External economy					
Exports, f.o.b.	215.0	226.0	355.1	376.5	378.3
Imports, f.o.b.	-251.1	-212.0	350.0	382.9	373.9
Current account balance	-80.8	-56.2	-54.3	-58.2	-34.5
Capital account balance	-137.6	-50.4	-10.2	62.8	51.6
Gross official reserves	162.7	90.9	128.1	147.2	156.3
Current account balance (in percent of GDP)	-9.2	-8.1	-6.7	-6.2	-5.3
Change in real effective exchange rate (in percent) 3/	-3.5	-33.5	15.9	2.6	...
External public debt (in percent of GDP)	104.2	205.4	108.3	99.4	93.8
Public debt service (in percent of GDP)	9.3	18.5	7.7	6.4	5.3
			In percent of GDP 2/		
Financial variables					
Government revenue	10.9	12.1	14.7	14.8	15.2
Government expenditure and net lending	27.0	25.1	22.5	21.1	18.8
Primary fiscal balance	-11.2	-5.9	-2.1	-1.4	0.8
General government balance	-16.1	-13.1	-7.8	-6.3	-3.6
Change in broad money (in percent)	-15.5	32.3	16.8	-9.9	15.5
Interest rate (in percent) 4/	12.3	12.1	8.4	7.3	6.2

1/ IMF staff estimates.
2/ Unless otherwise noted.
3/ (+) = appreciation.
4/ 12-month rediscount rate.

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Press Information Notices Released and Article IV Consultations Concluded January–April

An IMF member may release a Press Information Notice (PIN) at any time after the conclusion of its Article IV consultation with the Executive Board. For the latest releases consult the IMF web site (http://www.imf.org).
Press Information Notices are compiled and published as *IMF Economic Reviews* every four months as follows:

Issue No. 1: January–April • Issue No. 2: May–August • Issue No. 3: September–December

	Consultation Concluded	PIN Released	*IMF Economic Reviews* Issue
Argentina	February 4, 1998	February 23, 1998	1998: 1
Armenia	February 6, 1998	March 12, 1998	1998: 1
Bahamas, The	March 13, 1998	March 31, 1998	1998: 1
Bahrain	March 4, 1998	—	—
Barbados	January 30, 1998	February 25, 1998	1998: 1
Belgium	February 23, 1998	March 3, 1998	1998: 1
Botswana	March 13, 1998	April 10, 1998	1998: 1
Brazil	February 11, 1998	March 13, 1998	1998: 1
Cameroon	January 7, 1998	January 21, 1998	1998: 1
Canada	January 30, 1998	February 19, 1998	1998: 1
Cape Verde	February 20, 1998	March 10, 1998	1998: 1
Chile	February 11, 1998	February 20, 1998	1998: 1
Costa Rica	March 18, 1998	—	—
Côte d'Ivoire	March 17, 1998	—	—
Czech Republic	February 13, 1998	March 6, 1998	1998: 1
Egypt	January 7, 1998	—	—
El Salvador	February 20, 1998	April 6, 1998	1998: 1
Equatorial Guinea	February 2, 1998	—	—
Guinea	April 3, 1998	April 29, 1998	1998: 1
Guinea-Bissau	March 6, 1998	March 26, 1998	1998: 1
Hong Kong SAR	January 26, 1998	February 16, 1998	1998: 1
Iran, Islamic Republic of	January 30, 1998	—	—
Israel	February 11, 1998	March 10, 1998	1998: 1
Italy	March 13, 1998	—	—
Jordan	April 24, 1998	—	—
Kuwait	October 15, 1997	February 3, 1998	1998: 1
Latvia	March 23, 1998	April 14, 1998	1998: 1
Lesotho	February 4, 1998	—	—
Malaysia	April 20, 1998	April 27, 1998	1998: 1
Maldives	January 26, 1998	—	—
Mali	December 22, 1997	April 1, 1998	1998: 1
Moldova	April 20, 1998	—	—
Morocco	March 6, 1998	March 31, 1998	1998: 1
Mozambique	April 7, 1998	April 30, 1998	1998: 1
New Zealand	November 7, 1997	January 12, 1998	1998: 1
Nicaragua	March 18, 1998	April 9, 1998	1998: 1
Norway	February 23, 1998	March 9, 1998	1998: 1
Papua New Guinea	January 23, 1998	—	—
Philippines	March 27, 1998	—	—
Poland	March 16, 1998	March 30, 1998	1998: 1
Singapore	February 20, 1998	March 16, 1998	1998: 1
Slovak Republic	February 13, 1998	—	—
Slovenia	January 9, 1998	January 26, 1998	1998: 1
Spain	March 16, 1998	April 6, 1998	1998: 1
Sudan	February 27, 1998	April 13, 1998	1998: 1
Switzerland	February 20, 1998	March 6, 1998	1998: 1
Togo	January 21, 1998	February 19, 1998	1998: 1
Uganda	April 8, 1998	—	—
Vietnam	February 2, 1998	—	—

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Press Information Notices Released May–December

The IMF began issuing Press Information Notices (PINs) in May 1997. Listed below are those that were released through December 1997; they are available at the IMF's web site (http://www.imf.org). Press Information Notices released from January 1998 on are being published as *IMF Economic Reviews* (see preceding table) as well as being released electronically on the IMF web site.

	PIN Released
Algeria	July 23, 1997
Antigua and Barbuda	December 17, 1997
Aruba	May 27, 1997
Austria	June 20, 1997
Belize	June 5, 1997
Bolivia	September 19, 1997
Bulgaria	July 29, 1997
Chad	July 15, 1997
Dominica	June 27, 1997
Dominican Republic	September 17, 1997
Estonia	December 24, 1997
Finland	July 23, 1997
France	November 4, 1997
Germany	August 29, 1997
Ghana	December 1, 1997
Grenada	October 22, 1997
India	July 16, 1997
Ireland	July 25, 1997
Jamaica	October 3, 1997
Japan	August 13, 1997
Lithuania, Republic of	July 14, 1997
Madagascar	October 28, 1997
Mauritania	August 27, 1997
Mongolia	September 3, 1997
Nepal	June 13, 1997
Netherlands	June 27, 1997
Pakistan	November 4, 1997
Panama	December 22, 1997
Paraguay	October 22, 1997
Portugal	November 7, 1997
Senegal	August 26, 1997
South Africa	August 25, 1997
Sri Lanka	August 5, 1997
St. Kitts and Nevis	June 26, 1997
St. Vincent and the Grenadines	December 17, 1997
Sweden	September 2, 1997
Tanzania	December 23, 1997
Tunisia	June 5, 1997
Turkey	August 5, 1997
United Kingdom	November 6, 1997
United States	August 4, 1997