INTERNATIONAL MONETARY FUND

Staff Country Reports

September 2005
IMF Country Report No. 05/350

Republic of Madagascar: 2005 Article IV Consultation—Staff Report; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for Republic of Madagascar

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2005 Article IV consultation with Republic of Madagascar, the following documents have been released and are included in this package:

- the staff report for the 2005 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on April 1, 2005, with the officials of Republic of Madagascar on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on May 17, 2005. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- a Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its June 1, 2005 discussion of the staff report that concluded the Article IV consultation.

- a statement by the Executive Director for Republic of Madagascar.

The document listed below has been or will be separately released.

Selected Issues Paper and Statistical Appendix

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to publicationpolicy@imf.org.

Copies of this report are available to the public from

International Monetary Fund • Publication Services
700 19th Street, N.W. • Washington, D.C. 20431
Telephone: (202) 623-7430 • Telefax: (202) 623-7201
E-mail: publications@imf.org • Internet: http://www.imf.org

Price: $15.00 a copy

International Monetary Fund
Washington, D.C.

This page intentionally left blank

INTERNATIONAL MONETARY FUND

REPUBLIC OF MADAGASCAR

Staff Report for the 2005 Article IV Consultation

Prepared by the Staff Representatives for the 2005 Consultation with the Republic of Madagascar

Approved by Thomas Krueger and Anthony R. Boote

May 17, 2005

- The 2005 Article IV consultation discussions were held in Antananarivo during March 21–April 1, 2005. The mission met with President Ravalomanana, the Minister of Finance and other senior government officials, the Governor of the Central Bank, and representatives from the Senate, the donors' community, the private sector, and NGOs.

- The staff team comprised Mr. Fayolle (head), Mr. Nassar and Ms. Allain (all AFR), and Ms. Khemani (PDR). Mr. Jahjah, the Fund's Resident Representative in Madagascar, participated in the work of the mission. Mr. Quintyn (MFD, mission chief for the Ex Post Assessment (EPA)) also participated in the discussions during the first three days of the mission.

- The last Article IV consultation was concluded in December 2002, IMF Country Report No. 03/6, January 9, 2003. At that time, Directors commended the authorities for taking measures to reestablish investor confidence following the 2002 political crisis, and urged them to consolidate the progress made in reinvigorating private sector growth and to improve the efficiency of the tax system and customs administration. They also called for a strengthening of the budget process and for a medium-term development plan, embedded in a coherent macroeconomic framework, which would include specific poverty reduction programs.

- Madagascar has accepted the obligations under Article VIII, sections 2(a), 3, and 4, and maintains no restrictions on the making of payments or transfers for current international transactions (Appendix I).

- Relations with the World Bank are summarized in Appendix II.

Contents Page

Appendices

EXECUTIVE SUMMARY

- **Growth performance has improved in recent years**. The economy grew by over 5 percent per year in real terms in 2003 and 2004. Over the medium-term, staff forecasts real GDP growth to average 6 percent, which falls between the high and low growth scenarios of the authorities' Poverty Reduction Strategy Paper (PRSP). Sustaining high levels of growth should help reduce income poverty, a key objective of the Millennium Development Goals (MDGs).

- **Inflation subsided in 2003, but rose sharply throughout 2004**. This increase reflected the depreciation of the exchange rate, increases in the world prices of rice and oil, the impact of two cyclones, and inconsistent implementation of monetary policy in early 2004. Inflation peaked at 30 percent in February 2005, before declining as the domestic price of rice started to fall.

- **Significant tax reform measures were implemented, particularly at customs, but revenue performance continues to be weak**. In spite of these efforts, the ad hoc exemptions granted in 2003 further eroded the revenue base. The authorities agreed on the need to gradually raise Madagascar's relatively low tax-to-GDP ratio.

- **Persistent weaknesses in public expenditure management have complicated budget execution**. Lack of expenditure control and extensive recourse to emergency spending procedures led to fiscal overruns in recent years. Efforts are underway to strengthen the budget process as well as public expenditure management, in order to improve the effectiveness of the budget as a poverty-reducing instrument.

- **Considerable uncertainty surrounds the medium-term outlook for the balance of payments**. Exports on the whole have performed well, but have become increasingly concentrated on clothing to the United States. The expiration of the Agreement on Textiles and Clothing (ATC) in early 2005 and the expected end of certain provisions of the African Growth Opportunity Act (AGOA III) in 2007 underscore the need to preserve and build on the competitiveness gains achieved in the wake of the exchange rate depreciation in 2004.

- **Some progress has been achieved in strengthening competition and improving governance**. Key public enterprises were either privatized or put under private management, although often with significant delays; prices in the petroleum sector were liberalized in 2004; and the fight against corruption has been accelerated.

- **Institutional capacity constraints continue to hinder the authorities' ability to formulate and implement macroeconomic policy**. The authorities should make capacity building a priority and ensure that their efforts in this area benefit from coordinated donor support.

- The authorities expressed strong interest in pursuing relations with the Fund in the form of a PRGF successor arrangement, a strategy also favored in the Ex Post Assessment Report.

I. Introduction

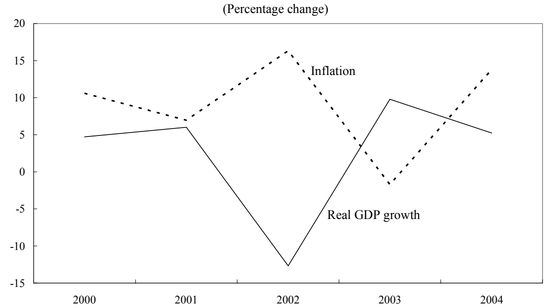
1. **The Article IV consultations took place against the backdrop of renewed political stability and rising inflation concerns**. While the country's economic performance improved in recent years, the economy remains vulnerable to shocks, including cyclones, and policy slippages. Political stability has been broadly restored, following the disputed 2001 presidential elections and the ensuing political crisis. However, the legacy of the crisis remains vivid, with some opposition leaders still in jail (without trial) or in exile. The second 3-year Poverty Reduction and Growth Facility (PRGF) arrangement expired in March 2005 and an ex post assessment was carried out to assess the Fund's long-term engagement in the country.

2. **The authorities' response to past Fund policy advice has been mixed**. In the context of the PRSP, they have prepared a medium-term development plan, which includes specific poverty reduction programs, and have taken measures to improve tax and customs administration. However, progress in revenue mobilization and in strengthening the budget process has been limited. This reflects persistent weaknesses in public expenditure management, as well as limited institutional capacity. The Ex Post Assessment Report, www.imf.org, discusses these issues in more detail.

II. Recent Economic Developments

3. **Real GDP growth was strong during 2003-04, but real per capita GDP remained below its pre-2002 level**. Following the civil-strife related economic slump of 2002, the recovery in 2003 was broad based (Figure 1); the tertiary sector, in particular, rebounded strongly. In 2004, despite the impact of two cyclones that hit the island in the first quarter of the year and a surge in inflation, real GDP growth is estimated to have reached 5.3 percent, buoyed by strong performance in the agricultural, construction, tourism, transport, and the Export Processing Zones (EPZ) sectors. This performance notwithstanding, real per capita GDP at end-2004 is estimated at about 92 percent of its 2001 level.

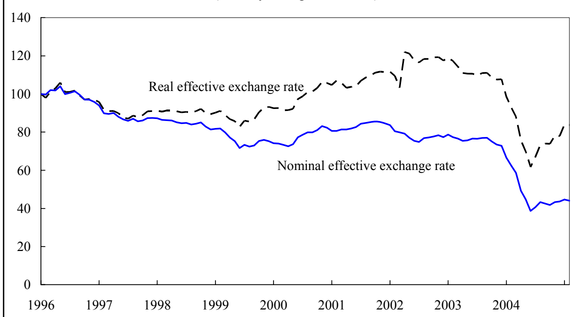
Figure 1. Madagascar: Real GDP and Inflation, 2000-04
(Percentage change)



Source: Malagasy authorities.

4. **Macroeconomic developments were dominated by a sharp depreciation of the Malagasy franc**. The exchange rate depreciated by about 50 percent against the euro in the first half of 2004 (Figure 2), owing mainly to (i) strong imports due to higher petroleum prices, increased government capital expenditures, and an acceleration of private imports in response to tax and tariff exemptions granted for imports of capital goods and selected other items in August 2003; and (ii) weak exports, as a result of two cyclones that damaged the vanilla and shellfish industries. The exchange rate stabilized during the third quarter of 2004, as import demand weakened and the government implemented important adjustment measures, and has remained stable since then.

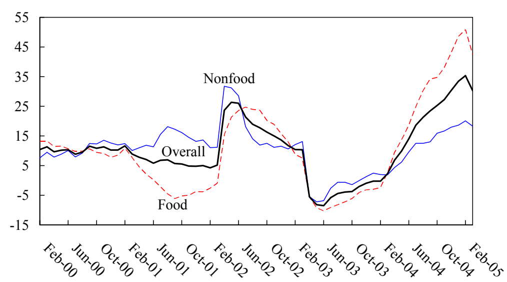
Figure 2. Madagascar: Real and Nominal Exchange Rates, January 1996 – February 2005
(Monthly average, 1996=100)



Source: INS: *Information Notification System*.

5. **Inflation subsided in 2003 but has picked up sharply since the beginning of 2004**. Year-on-year consumer price inflation, after falling by about 1 percent in 2003, accelerated in 2004 and early 2005 (Figure 3). The sharp depreciation of the exchange rate in late 2003/first half of 2004 and the near doubling of the price of rice and of petroleum products were the main factors driving inflation. Inflation continued to rise in early 2005, reaching 30 percent in February 2005 (on a year-on-year basis) before declining to 27 percent in March, as the domestic price of rice eventually started falling.

Figure 3. Madagascar: Consumer Price Index,
February 2000–March 2005
(Percentage change, year–on–year basis)



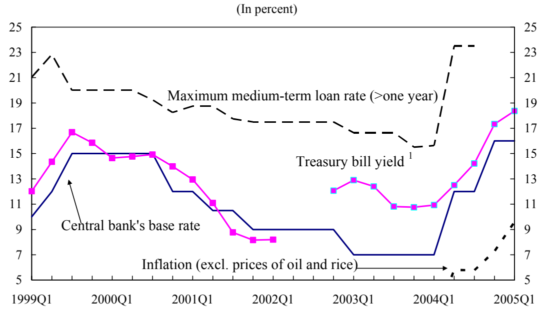
Source: Malagasy authorities.

6. **Monetary policy has been tightened in the course of 2004 to help contain inflationary pressures**. In 2003, the Central Bank of Madagascar (BCM) pursued an expansionary monetary policy, following the economic slump in 2002, with a view to accelerating the recovery of economic growth. The BCM responded slowly and inconsistently to the sharp exchange rate depreciation and intensifying inflationary pressures in early 2004.[1] Nonetheless, the successive tightening measures taken since April 2004[2] led

[1] Inconsistent implementation of monetary policy and inadequate coordination between the Ministry of Finance and the BCM sometimes led to erratic liquidity management (see Staff Report for the fifth review, IMF Country Report No. 04/404, December 10, 2004.

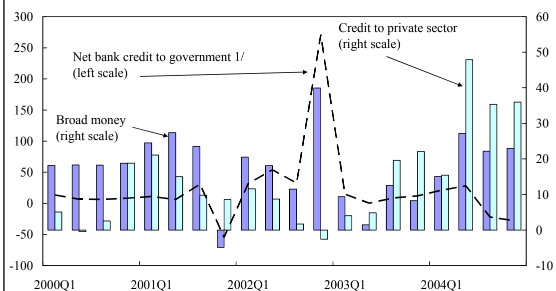
to a significant increase in interest rates (Figure 4, attached, and Figure 5), thus keeping interest rates substantially higher than inflation (excluding rice and oil prices). In spite of these measures, broad money growth (as measured by M3, including foreign currency deposits), which had started to decelerate (on a year-on-year basis) since August, increased sharply in December (Figure 6). This reflected inter alia the accumulation of net foreign assets by the BCM and a strong increase in credit to the private sector. The increase in credit to the private sector has been driven mainly by credit to privately owned oil companies, following the liberalization of the sector in 2004.

Figure 5. Madagascar: Weighted-Average Interest Rates, 1999:Q1–2005:Q1
(In percent)



Source: Central Bank of the Republic of Madagascar (BCM).
[1]No treasury bill auctions were conducted during March-September 2002.

Figure 6. Madagascar: Money and Credit Developments, 2000Q1-2004Q4
(12-month percentage change)



Source: Malagasy authorities.
1/ Excludes the takeover of the oil company, SOLIMA, debt.

7. **Financial soundness indicators have improved since the 2002 economic slump**. Profitability and prudential indicators for the banking sector have improved in recent years and banks appeared to be adequately capitalized and liquid (Text Table 1). The ratio of nonperforming loans (NPLs) to total gross loans fell from 19.6 percent in 2002 to 11.4 percent in 2004. This reflects not only a decline in NPLs, but also the rapid rise in credit. Furthermore, the exposure of foreign banks to a few "niche" borrowers and use of guarantees provided by their headquarters have increased in recent months. A Financial Sector Assessment Program (FSAP) mission scheduled for first half of 2005, with a first mission fielded in April, will examine these issues.

[2] The BCM raised its base rate in April, June, and September 2004, increased the reserve requirement rate in three steps, including by broadening the reserve base in April 2004 and again in March 2005, and has held reverse auctions since mid-2004.

Text Table 1. Bank Soundness Indicators, December 1998 - 2004

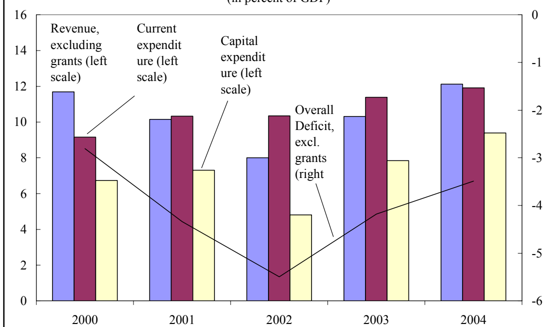
	1998	1999	2000	2001	2002	2003	2004
Capital adequacy			(Ratio; in percent)				
Regulatory capital to risk-weighted assets							
Lowest ratio	8.6	9.7	10.1	12.0	11.4	10.7	7.2
Highest ratio	30.5	28.7	32.2	34.1	38.7	38.5	31.3
Asset quality							
Nonperforming loans to total gross loans	21.1	8.4	8.4	10.3	19.6	16.7	11.4
Earnings and profitability							
Return on assets	3.2	4.3	4.0	2.8	1.1	3.2	4.0
Return on equity	91.0	53.0	47.0	39.0	16.0	45.7	64.6
Noninterest expenses to gross income	46.5	42.9	45.4	48.9	52.2	46.9	44.8
Personnel expenses to noninterest expenses	44.6	36.7	38.4	35.3	38.3	38.9	35.4
Liquidity							
Liquid assets to total assets	35.9	37.0	36.9	44.2	52.1	50.5	47.6
Liquid assets to short-term liabilities	61.9	61.2	62.2	70.0	77.8	73.2	67.8
			(In billions of Ariary)				
Memorandum items:							
Total assets	844.4	986.2	1,133.6	1,344.6	1,393.0	1,536.5	2,011.6
Total profits before tax	27.4	42.8	45.3	37.3	15.9	49.9	80.2
Foreign exchange exposure limit (highest ratio)	...	...	...	17.2	19.6	58.3	127.2

Source: Banking and Financial Supervision Commission, Central Bank of Madagascar (BCM).

8. **Implementation of the main recommendations of the Stage One Report of the Safeguards Assessments continued in 2004 with help from the Monetary and Financial Systems Department (MFD)**. In line with the recommendations of the safeguards assessment, the central bank (i) published its complete audited financial statements for 2003 in December 2004; (ii) adopted a new accounting framework effective January 1, 2005; and (iii) is in the process of completing the documentation of its internal control system for reserve management and foreign exchange related activities. In addition, an anti-money laundering legislation adopted in 2004 became operational in 2005.

9. **Despite the implementation of significant reforms at customs, revenue performance continued to be weak**. The tax base remains narrow, reflecting the lack of progress toward inclusion in the tax net of key sectors whose contribution to the tax effort is currently very low (such as tourism and mining) and the proliferation of exemptions.[3] However, significant reform measures were implemented at customs, including the acceleration of customs clearance procedures, and the strengthening of ex post controls through increased use of a risk management system. Nonetheless, the revenue-to-GDP ratio continued to stagnate, reaching 10.9 percent in 2004, close to the authorities' objective, but below the level reached at the turn of the millennium and that of similar African countries (Figure 7 and Text Table 2).[4] Preliminary information indicates that this disappointing trend continued in the first quarter of 2005.

Figure 7. Madagascar: Fiscal Developments, 2000-04
(in percent of GDP)



Source: Malagasy authorities.

Text Table 2. Fiscal Revenue in Selected African Contries, 1990-2004
(in percent of GDP)

	Benin	Madagascar	Malawi	Niger	Sub-Saharan Africa
1990-1994	12	9.8	18.9	8.1	19.8
1995-1999	15.1	9.8	16.9	8.3	20.7
2000-2004	16.5	10.5	19.8	9.8	22.4

Source: WEO.

10. **Persistent weaknesses in public expenditure management have complicated budget execution**. Current primary expenditure overruns reached 0.8 and 0.5 percent of GDP in 2003 and 2004, respectively, reflecting extensive recourse to emergency spending procedures in both years. Insufficient control over expenditure undertaken by decentralized government bodies and public entities also contributed to the 2004 outturn.[5] Nonetheless, total government expenditure has been contained, as the overruns in some areas were partially offset by lower investment outlays in 2003, and by the reining in of other expenditures, particularly wages, in 2004. As a result, the domestic balance improved by 1 percent of GDP in 2004,[6] and the government was able to reduce its domestic indebtedness in an amount equivalent to 2.8 percent of GDP.

---

[3] In August 2003, tax and tariff exemptions were granted by law on a large array of capital and selected other commodities. Originally envisaged to last two years, they were partially rescinded in August 2004, and will be fully eliminated in September 2005.

[4] Comparator countries were chosen based on the share of agriculture in GDP, and their development level, proxied by real per capita GDP.

[5] These operations are recorded as treasury operations in the fiscal tables.

[6] At the same time, the overall deficit widened by 0.9 percent of GDP, following higher-than-expected foreign financed investment.

11. **In spite of the sharp depreciation of the exchange rate, the current account deficit widened considerably in 2004**. Even though EPZs and tourism related activities performed strongly following the depreciation of the exchange rate, the current account deficit (excluding grants) widened from 8 percent of GDP in 2003 to 14 percent of GDP in 2004, reflecting a sharp decline in the volume of vanilla exports which were affected by the cyclones in early 2004. In addition, imports of equipment increased by about 60 percent, following the tax and tariff exemptions granted in August 2003. The current account deficit was financed mainly by external loans and capital grants. In spite of an accumulation of SDR 49 million, gross international reserves remain low, amounting to about 2.8 months of imports.

Text Table 3. Madagascar: Exports of Clothing to the United States, 1990-2003
(In millions of U.S. dollars)

	1990	1992	1995	2000	2001	2002	2003
Total imports	0.4	0.3	7.3	115.7	188.7	97.3	212.1
o/w AGOA					178.1	89.4	196.0
o/w Third Party Provision					72	69	172

Source: COMTRADE, United States Commerce Dept. website on AGOA Trade Statistics

12. **Exports on the whole have performed well, but have become increasingly concentrated on clothing exports to the United States**. Madagascar has traditionally had a diverse export base. Over the last few years, traditional exports, including agricultural exports, have shown weak growth. However, exports of clothing, especially to the United States have performed well, benefiting from the third party provision of the African Growth Opportunity Act (AGOA III) (Text Table 3). As a consequence, the U.S. market share of the total value of exports has increased by half since 1990, and reached 30 percent in 2003.

13. **Progress, albeit slow, has been achieved in implementing key structural reforms**. Significant progress has been achieved in structural reforms aimed at lowering the cost of doing business. Madagascar has streamlined its legal requirements for setting up private sector business, and introduced a one-stop center for all prospective investors. In addition, the authorities have revised the land law to allow foreigners limited access to land ownership in Madagascar and the mining code to attract corporate investors into the sector. Some progress has also been achieved in the fight against corruption, and a new anti-corruption bureau was established in October 2004. However, progress on public enterprise reform was slow. After considerable delay, the telecommunications company (TELMA), the cotton company (HASYMA), and the sugar company (SIRAMA), have been either privatized or put under private management in 2004. A private company has been selected to manage the

utility company (JIRAMA) starting in the first half of 2005, although the medium-term strategy for the sector is yet to be defined.

III. Ex Post Assessment (EPA) Discussions

14. **The report on the Ex Post Assessment of the Fund's long-term engagement with Madagascar was discussed with the authorities in the context of the 2005 Article IV consultation**. The authorities were in broad agreement with the analysis and recommendations of the report. They hoped that the Fund would engage in discussions on a successor arrangement in view of the country's continuing balance of payments and development needs. They agreed that the main challenge facing Madagascar is to achieve higher economic growth rates necessary to reduce poverty significantly, and recognized the importance of improving domestic revenue mobilization, although there was some discussion on the best strategy to reach this goal (see paragraph 26 below). The authorities also hoped that, with a possible new program, a closer partnership would develop between Madagascar and the Fund. They indicated that ownership of Fund-supported programs had increased significantly in recent years, and felt the Fund did not always adequately explain the rationale for policy measures proposed under the program in the past. They also emphasized the need for continued technical assistance to support their capacity building efforts. The international donor community and representatives of NGOs, on their part, expressed their desire for continued Fund involvement in Madagascar, noting its anchor role in instilling macroeconomic discipline.

IV. Economic Prospects And Risks

15. **Madagascar's poverty reduction strategy paper (PRSP) presents two growth scenarios for the period 2004-06**. The PRSP presents a high growth scenario of 7.5 percent and a low growth scenario of 4.5 percent. The high growth scenario assumes that the private sector savings rate and the absorptive capacity of the economy will increase sharply, which would allow for a higher level of domestic investment and result in a large budget deficit (including grants). The low growth scenario assumes that the rate of project implementation, investment productivity, and the flow of foreign resources will be the same as the 1999-2003 average (excluding 2002). The PRSP envisages inter alia promotion of good governance and significant increases of public expenditure on priority sectors, such as education, health, and road infrastructure.

16. **There was broad agreement on economic prospects for 2005**. The authorities concurred with staff's projection of 6.3 percent real GDP growth in 2005. This reflects strong growth in agriculture, tourism, and construction sectors. Fiscal consolidation is expected to continue, in line with the 2005 finance law projections, with the revenue performance reaching 11.4 percent of GDP and expenditures being contained, thus allowing for a

1.7 percent of GDP improvement in the domestic balance.[7] This fiscal stance and continued tight monetary policy are expected to contribute to a fall in inflation to 7 percent at end-2005 (on a year-on-year basis). Exports of goods and services (tourism in particular) are projected to pick up and the volume of imports to slow down temporarily, following its sharp increase in 2004. The current account deficit (excluding grants) would decline to 11.5 percent of GDP in 2005. However, due to lower foreign financing relative to 2004, gross international reserves are expected to fall marginally to 2.7 months of imports in 2005.

17. **Over the medium-term, real GDP growth is projected by staff to average 6 percent, which falls between the high and low growth scenarios of the PRSP**. These projections assume that both private and public investment would decline slightly relative to GDP following the sharp increase in 2004 investment. It is also assumed that Madagascar will remain politically stable, maintain sound macroeconomic policies, improve governance, continue reforms of the business environment, and attract relatively high levels of foreign direct investment and donor assistance (including from the Millennium Challenge Corporation (MCC), see Box 1). Growth would be spurred by strong performance in the agricultural, agro-based industry, construction, mining, and tourism sectors. The PRSP, which is being updated in the context of a second annual progress report, is expected to be in line with these assumptions.

18. **The budgetary framework for the medium term envisages further fiscal consolidation**. Revenue projections assume the successful implementation of a comprehensive reform of the tax system (which would result inter alia in a significant widening of the tax base), as well as a buoyant macroeconomic environment. At the same time, expenditures are expected to be contained, while allowing for a gradual increase in domestically financed investment outlays and higher poverty spending, resulting in the buildup of a small domestic surplus in the outer years.

19. **The external outlook is expected to improve in the medium term**. The projections reflect a sharp deceleration in the growth of textile exports in 2005, in large part due to the impact of the expiry of the Agreement on Textiles and Clothing (ATC), and a further deceleration in 2006 due to the expected termination of AGOA III provisions in 2007. Thus, significant balance of payments needs are expected to continue. However, some improvement in the current account is envisaged in the medium term, due to a pick-up in export activities, especially in the tourism and EPZ sectors, in response to the recent gains in competitiveness. External financing requirements will remain relatively high due to the country's large infrastructure needs, but the authorities are committed to borrowing only on concessional terms. These developments, together with growth in private transfers, would allow Madagascar to accumulate international reserves equivalent to about 4 months of imports by 2009.

---

[7] At the same time, priority spending is foreseen to increase substantially. For example, health expenditures are projected to increase by 40 percent compared to the 2004 outturn.

Box 1. The Millennium Challenge Corporation and Madagascar

The Millennium Challenge Corporation (MCC) was established by the U.S. Government in 2004 to provide development assistance in the form of grants to low-income countries that rule justly, invest in their people, and encourage economic freedom. Madagascar is the first country to sign an agreement with the MCC. This agreement, signed in April 2005, includes projects in the amount of US$110 million over a period of four years, covering the following three areas that are considered important for growth and poverty reduction in Madagascar:

Land tenure: The current backlog of requests for land titles cannot be processed due to lack of resources and cumbersome registration procedures. This, in turn, impedes rural investment, land development, expansion of collateral-based lending, and agricultural productivity growth. The project should increase land titling and security and improve the efficiency of land service administration.

Financial sector development: The project is designed to: (i) promote legal and regulatory reforms, with particular focus on capital markets and competition in commercial banking; (ii) strengthen sovereign debt management and issuance, including extending the yield curve and broadening access to the Treasury bill market; (iii) strengthen the national savings bank, by reducing transaction costs; (iv) promote new financial instruments for financing agriculture, including working capital for farmers; (v) improve the payments system; and (vi) improve the quality of demand for credit, including the establishment of a credit information bureau, and training for microfinance institutions.

Agricultural business investment: A key element of Madagascar's agricultural development strategy is to assist farmers in transitioning from subsistence farming to market agriculture. The MCC will help enhance research, provide access to improved technologies, farm management and business planning, infrastructure development, and policies to enhance productivity and returns to investment.

20. **The external debt position remains fragile**. The updated debt indicators remain broadly in line with projections presented in the completion point document www.imf.org albeit at slightly lower levels (Table 1).[8] The ratio of debt to exports falls below the level of the HIPC thresholds only after the delivery of additional bilateral debt relief beyond the HIPC Initiative. The authorities are making strong efforts to obtain full HIPC Initiative

[8] A fully updated debt sustainability analysis (DSA), prepared jointly with the Bank, is expected to be carried out later in 2005, as Madagascar falls in the transition period under the guidelines for the presentation of jointly agreed Fund/Bank DSAs.

assistance. They have contacted all the non-Paris Club creditors and are well advanced in their negotiations with Paris Club creditors, including on additional debt relief. They also intend to strengthen debt management capacity, particularly through enhanced coordination between the Treasury and the central bank.

21. **There are several risks to the medium-term outlook**. First, as illustrated by past slippages, reforms envisaged in the PRSP may not materialize due to political pressure from vested interests. Second, the external outlook is subject to considerable uncertainties as (i) prices of vanilla—Madagascar's main traditional export commodity—may fall by more than projected;[9] (ii) the impact of the expiry of the ATC could be larger than expected in 2005; and (iii) the termination of the third party apparel provision of AGOA, scheduled for September 2007, may be more damaging than projected to the textile market. The concentration of exports over the past few years in clothing renders the balance of payments particularly vulnerable. On the other hand, larger amounts of external assistance and foreign direct investment, together with appropriate measures to increase absorptive capacity, could lead to higher GDP growth rates over the long run.

V. Policy Discussions

22. Considerable progress has been made in stabilizing the economy and laying the foundation for higher growth, but daunting challenges remain if income poverty is to be significantly reduced in coming years. Achievement of this goal requires a more efficient expenditure management to ensure that public resources contribute effectively to realizing the other MDGs. Policy discussions focused on: (i) policies to maintain macroeconomic stability and improve the economy's resilience to shocks; (ii) measures to improve competitiveness; (iii) public expenditure management; and (iv) data issues and capacity building.

A. Maintaining Macroeconomic Stability and Improving Resilience to Shocks.

23. **The authorities concurred that inflation remains a key concern for macroeconomic stability**. While the price of rice has begun to fall in March 2005 and is expected to decline further in the coming months, the deflationary impact of this decrease could be partly offset by the effects of oil price increases. The authorities revised the inflation target for end-2005 upward from 5.5 percent to 7 percent to reflect the impact of higher oil prices. In the staff's view, this revised target is achievable, provided that the envisaged tight monetary and fiscal policies are fully implemented, and that oil prices moderate and rice

[9] While a sharp decline is factored into the medium term projections of vanilla prices as a result of global excess supply, early 2005 transactions took place at even lower prices.

prices decline in the coming months.[10] In this context, the authorities continue to monitor monetary developments closely and stand ready to raise interest rates further, should inflationary pressures not abate. They are also determined to make every effort to ensure that the improvement of the domestic fiscal balance by 1.7 percent of GDP foreseen in the 2005 finance law materializes. In particular, they are of the view that the strict implementation of the revenue enhancing measures discussed with staff (Box 2) will allow them to meet their revenue target for 2005, in spite of the disappointing first quarter outturn. The authorities are confident in their ability to keep expenditures in line with available resources, and have already started implementing measures to this effect (see Section C below). Staff stressed that the authorities' 2005 fiscal targets were ambitious and required full implementation of the revenue measures and strengthened expenditure control. The decision to limit statutory advances from the BCM to 10 percent of the previous year's tax revenue, down from 15 percent under the previous agreement, was welcome.

Box 2. Revenue Measures in 2005

At customs, measures include:

- Collapse of the two remaining trade taxes—customs duties and import taxes—into one;
- Elimination of the customs duties advance scheme as of January 2005;
- Strengthened use of the risk management system, in order to increase the selectivity of controls and accelerate the customs clearing process;
- Effective use of the new ASYCUDA ++ software in the main port starting April 1, 2005 and progressive deployment to the 5 largest customs bureaus by August 2005; and
- Mandatory payment of customs duties through the banking system, effective in April 2005.

At the tax directorate, measures include:

- Intensification of tax inspections through the systematic use of data generated by other financial administrations, in particular customs, the treasury, and the public procurement office;
- Effective use of the new tax management software by end-June 2005;
- Intensification of inspection and strengthened collection procedures for excise taxes; and
- Launching of an inspection campaign in the tourism sector.

24. **The authorities recognized the need to improve the effectiveness of monetary policy**. Developments in 2004 have shown that the instruments currently available to the BCM could be used more effectively to achieve monetary policy targets. Against this

[10] See Chapter I of the Selected Issues Paper for an empirical study undertaken by staff on determinants of inflation in Madagascar.

background, the authorities intend to implement the recommendations of a recent MFD technical assistance mission, regarding (i) the development of indirect monetary policy instruments. In particular, they have agreed to gradually convert the securitized government debt held by the BCM into marketable securities; (ii) the operational framework for liquidity forecasting and management; (iii) further enhancement of the coordination with the Treasury; and (iv) the development of the money market.

25. **The authorities are committed to strengthening banking supervision and the contribution of the financial sector to economic growth**. The recent appointment of the members of the Banking Supervision Commission (CSBF) should help ensure that the prudential regulations are strictly adhered to by all banks, but the CSBF continues to have staffing problems and it has not yet been able to carry out on-site inspections owing to a lack of qualified staff. In this regard, the authorities indicated that they have established an action plan for 2005. The CSBF has also begun to establish closer cooperation with the supervisory agencies in foreign banks' home countries. Moreover, the development of the financial infrastructure is a priority to be supported by donors, including the Fund, the World Bank, and the MCC. A law establishing the legal framework for microfinance operations is to be approved by Parliament later in 2005.

26. **The authorities agreed that improving revenue mobilization remains key to enhancing macroeconomic stability, but acknowledged that conflicting views about the goals of fiscal reform hinder progress**. The lack of consensus on a reform strategy for the tax system, and particularly for domestic taxes, still prevents the revenue-to-GDP ratio from reaching levels attained by similar African countries. In turn, the difficulties in adhering to reform objectives reflect the persistence of conflicting opinions about the role of the tax system. At the center of the debate is the perceived contradiction between the need to raise fiscal revenue and the desired increase of private investment flows to stimulate private sector growth. In this context, the authorities were of the view that the expected effects on economic activity of granting special fiscal incentives often outweigh the implied losses in tax revenue, as evidenced by the August 2003 exemptions. Staff stressed that the uneven success of the EPZ strategy in certain sectors pointed to the limitations of the special tax incentives strategy to attract investors. The opportunity cost of the tax expenditure associated with the various exemptions also had to be weighed against that of other public expenditures, particularly those addressing important public investment needs. Moreover, the existence of multiple exemptions created economic distortions and encouraged rent seeking behavior. Staff stressed the importance of having a coherent, simple, and predictable tax system in place, and urged the authorities to reach a consensus on clear reform goals which would support the revenue objectives envisaged in the medium term.

B. Competitiveness

27. **Madagascar's competitiveness improved significantly in 2004, but there has been some reversal in recent months**. A study undertaken by staff indicates that while the current level of the real effective exchange rate is below its long-run fundamentals, deviations from the long-run trend can be explained for the most part by terms of trade, productivity, and

monetary policy shocks.[11] Under these circumstances, at its current level, the real effective exchange rate seems broadly appropriate—a view broadly shared by the authorities.

28. **While Madagascar's competitive position benefits from low labor costs, other cost factors and low productivity tend to weaken prospects for the tradable sector**. An important competitiveness advantage for Madagascar comes from the low nominal wages; but some detailed sector specific indicators show that this advantage is partly eroded when adjusted for productivity. Non-wage costs such as those related to electricity, transportation, and communication also appear to be relatively high.[12] The government is cognizant of these problems and has taken measures to improve competitiveness, including the implementation of an infrastructure program (with donor support). The authorities also intend to promote diversification of the export base, and stressed that the expansion of the agro-business sector was a key element of their development strategy.

29. **Staff supported the authorities' view that the flexible, market-determined exchange rate should be maintained**. The introduction of a new continuous interbank foreign exchange market in July 2004 has contributed to the stabilization of the exchange rate in recent months. Staff encouraged the authorities to intervene only in the foreign market to dampen sharp swings in the exchange rate and to meet the central bank's objective of net foreign asset accumulation, consistent with the BCM's operational guidelines for its interventions in the foreign exchange market.

30. **Expanding external trade is an integral part of the authorities' development agenda**. In the past couple of years, the four trade taxes were collapsed into one, the number of tariff rates was reduced from 7 to 4, and the highest rate was lowered from 33 to 25 percent.[13] The authorities have also started to reduce some of the royalties imposed on selected imported goods (mainly tobacco, alcohol, sugar, and dairy products). Moreover, Madagascar is currently a member of the Common Market for Eastern and Southern Africa (COMESA) and it is to become a member of the Southern African Development Community (SADC) by the end of 2005. Despite the differing and potentially conflicting trade regimes, the authorities expect membership in SADC to open new markets and bring new investment into Madagascar. Staff argued that efforts to deepen regional integration should be firmly set within a framework of multilateral liberalization. The authorities are aware of the complexity of dealing with two different regimes at customs, but on balance held that implementation would be fairly straightforward.

---

[11] See Chapter II of the Selected Issues Paper for a study on the real effective exchange rate.

[12] See Chapter III of the Selected Issues Paper for a study on competitiveness and export performance.

[13] As a result of these changes as well as the effect of the tariff exemptions granted in September 2003 for a period of two years, the average weighted tariff is estimated to have declined from 22 percent in 2001 to 13.4 percent in 2004.

31. **Improving governance is a key element of the authorities' development strategy**. The authorities underlined that the measures recently taken to fight against corruption and reform public enterprises have contributed to improving the business climate. Increased transparency and accountability in the conduct of public affairs are also expected to contribute to raise Madagascar's attractiveness to investors.

C. Public Expenditure Management

32. **The authorities concurred that strengthening public expenditure management is needed to enhance the efficacy of the budget to achieve stated policy goals**. Measures implemented with the 2005 finance law include the transfer of the budgetary oversight for the military wage bill to the Ministry of Finance and the elimination of the emergency spending procedure. The authorities were of the view that the audit report on the expenditures incurred through this procedure in 2004, which is being finalized, should also provide useful recommendations on further ways to avoid future slippages. Furthermore, a committee has recently been set up within the Ministry of Finance to ensure a better alignment of expenditure commitments to available resources, while preserving poverty reduction expenditures. At the same time, the Treasury is looking into ways to strengthen fiscal reporting by public entities and decentralized government bodies in order to avoid the recurrence of the expenditure overruns that took place in 2004. The authorities are also in the process of compiling a single, comprehensive action plan to strengthen the budgetary process based on the results of the various diagnostic studies on public expenditure management undertaken in recent years. The plan, which is prepared in consultation with donors, would cover the entire budget cycle (see Box 3), and aims, inter alia, at improving the alignment of the budget with PRSP priorities.

33. **The switch to performance budgeting has revealed several weaknesses, which the authorities are beginning to address**. In particular, weak monitoring procedures for foreign financed investment and the very high number of output indicators (close to 1,500 in total) complicate the implementation of the different programs. The medium term expenditure framework (MTEF) should also be strengthened, and integrated in a fully consistent macroeconomic framework. The authorities concurred with staff on the need to address these issues in order to ensure that the transition to performance budgeting proceeds smoothly. In the meantime, they indicated that they would maintain safeguard procedures and continue to monitor budget execution on a line-item basis.

D. Capacity Building and Data Issues

34. **The authorities agreed with the mission that strengthened administrative capacity is key to ensure successful implementation of their reform agenda**. They recognized the need to develop a time-bound action plan to enhance administrative capacity in the areas of public debt management, expenditure execution and control, tax and customs administration, revenue mobilization, monetary management, and interventions in the foreign exchange market. Even though Madagascar received Technical Assistance in the past in most of these areas, including from the Fund (see Appendix I), a lot more remains to be

accomplished. The mission encouraged them to approach their main development partners as soon as the action plan is finalized, to ensure its implementation is adequately coordinated.

35. **Economic data shortcomings in several areas hamper surveillance**. As indicated in Appendix III, Madagascar's database remains weak, particularly for the real sector, government finances, the balance of payments, and social indicators. Madagascar is a participant in the General Data Dissemination System (GDDS), and its metadata are posted on the Data Standards Bulletin Board. Staff urged the authorities to include all identified needs in the statistical area in the above mentioned capacity building action plan.

Box 3. Measures to Strengthen Public Expenditure Management

- **Budget preparation**: its calendar has been revised starting in 2005 to involve at an early stage the line ministries in the budgetary discussions and improve the alignment of the budget with PRSP priorities. The medium-term expenditure framework (MTEF) will be strengthened to ensure that the medium-term sectoral strategies are set within a consistent macroeconomic framework.
- **Budget execution**: the quality and fluidity of budget execution is expected to be improved by the elimination in 2005 of emergency spending procedures, and the merger of the sub-authorizing officer and appropriations manager activities should simplify and accelerate the expenditure system. The program budgets will be rationalized, and their consistency with the PRSP indicators enhanced. Procedures for monitoring foreign financed investment and reporting requirement for public entities and decentralized government bodies will be strengthened. Further improvement is also needed in the areas of cash management, accounting procedures, and treasury operations, for which technical assistance has been requested.
- **Internal and external controls**: the decree on supporting documentation for expenditure authorization is being implemented, and the General Finance Inspectorate is expected to become operational by end-June.
- **Procurement issues**: the implementation decrees for the new procurement code are expected to be finalized by July 2005.

VI. Staff Appraisal

36. **Madagascar's recent growth performance is commendable, but major uncertainties surround the medium-term prospects**. Following the 2002 political crisis, economic activity has rebounded in 2003-04. However, sustaining growth rates consistent with achieving the Millennium Development Goals will require the implementation of macroeconomic and structural policies that preserve competitiveness, strengthen governance, and attract private investment.

37. **Inflation increased throughout 2004 and remains a key concern for 2005**. The 7 percent year-on-year inflation target for end-2005 is achievable, but this will depend on the evolution of the world prices of oil and rice, as well as the steadfast and timely implementation of the envisaged tight monetary and fiscal policies. Recent measures to

improve the coordination within the Ministry of Finance and between the Ministry of Finance and the BCM are welcome.

38. **A coherent and predictable tax policy would help achieve the revenue target**. Ad hoc revisions to the tax and tariff system need to be avoided in the future especially when such revisions lead to a further erosion of revenue collection, which is low by international comparison. The uneven success of the EPZ strategy in certain sectors indicates that the success in attracting investors does not necessarily imply major tax incentives. A more comprehensive approach, which ensures that reductions in the tax rates are matched by a broadening of the tax base, seems more appropriate. Achieving the revenue-to-GDP target of 11.4 percent in 2005 appears ambitious and will require the strict and timely implementation of the envisaged measures.

39. **Public expenditure management needs to be strengthened with donor support**. The fiscal slippages that took place in 2003 and again in 2004 reflect a lack of expenditure control, especially in the decentralized government entities. Strengthening the budgetary process is crucial to maintain donor confidence and ensure the effectiveness of the budget as a poverty-reducing tool, and the authorities' determination to avoid the recurrence of such slippages and accelerate the ongoing public expenditure reforms is welcome. The measures already taken to address the weaknesses identified during the 2004 budget execution, including a better control of military wages, constitute clear evidence of this determination.

40. **Further steps are needed to strengthen monetary policy implementation and banking supervision**. In particular, there is a strong case for the central bank to use its monetary policy instruments more effectively and be more proactive in managing liquidity, especially at a time when inflation needs to be brought under control. In addition, the authorities could draw on the recommendations of the ongoing FSAP to further strengthen banking supervision.

41. **The expiration of the ATC in 2005 and the expected end of AGOA III in 2007 reinforce the need to preserve and build on export competitiveness**. While the current level of the real exchange rate is broadly appropriate, structural reforms need to be pursued aggressively to strengthen competitiveness. Important progress has been made in lowering external trade barriers, and the authorities are encouraged to deepen regional integration within a multilateral framework. Moreover, the implementation of the public enterprise reform agenda needs to be accelerated. While progress has been achieved recently with the privatization of the state-owned telecommunications and cotton companies, a comprehensive strategy for the utilities sector is urgently needed, in consultation with the World Bank, as the weaknesses in the distribution of electricity are among the most frequently mentioned impediment to the business climate.

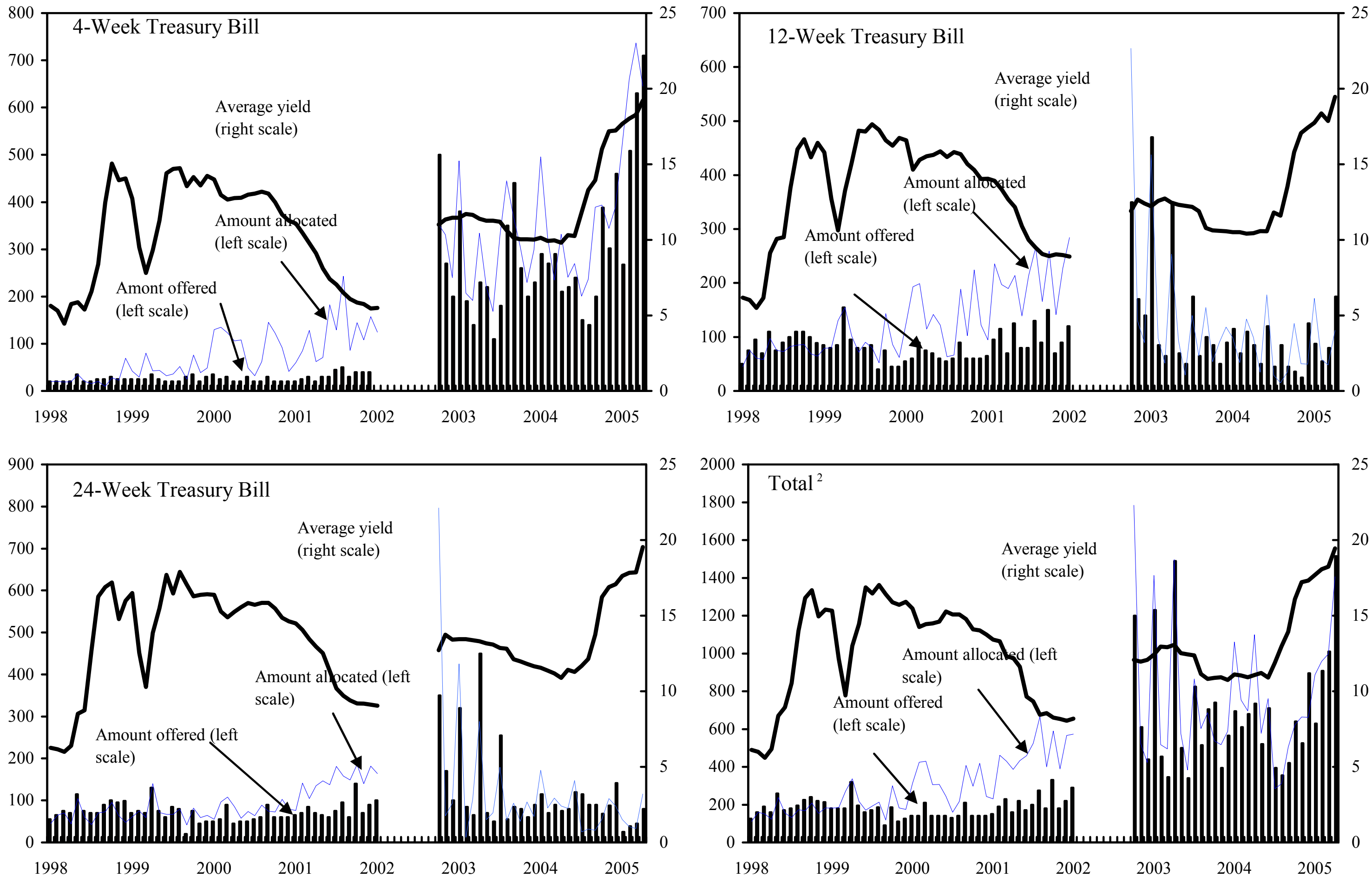
42. **Limited capacity continues to hinder the authorities' ability to implement their development program**. The authorities should finalize their action plan for capacity building, especially at the Ministry of Finance, the central bank, and the statistical institute in 2005. Moreover, shortcomings in economic and social data hamper policy formulation and

monitoring. A strengthening of the country's statistical capacity is urgently needed. Fully coordinated donor support will be key for success in capacity building.

43. **The staff concurs with the conclusion of the EPA report that a successor PRGF arrangement could assist the country in achieving its poverty reduction goals**. A new program would also help promote private sector led growth, at a time when the economy remains vulnerable and the level of reserves low. In particular, the experience from past arrangements points to the need to strengthen the revenue base, improve public expenditure management, accelerate capacity building efforts, and implement policies that maintain the country's competitiveness. The challenges ahead are considerable, but the authorities' ownership is encouraging, as evidenced by the successful implementation of the PRGF arrangement that expired in March 2005, the first under which all disbursements scheduled there under took place.

44. It is proposed that the next Article IV consultation with Madagascar will take place on the standard 12-month cycle.

Figure 4. Madagascar: Treasury Bill Auctions, January 1998 – April 2005[1]
(Left scale in billions of Malagasy francs; right scale in percent)



Source: Malagasy authorities.

[1] No treasury bill auctions were conducted during March-September 2002.
[2] Sum of the 4-week, 12-week, 24-week, and 52-week treasury bills.

Table 1. Madagascar: Selected Economic and Financial Indicators, 2003-09 [1/]

	2003	2004		2005	2006	2007	2008	2009
		Prog. [2]	Est.	Revised Projections				
	(Annual percentage change, unless otherwise indicated)							
National income and prices								
Nominal GDP growth	12.8	16.4	20.3	24.0	12.0	11.5	11.5	11.2
Real GDP growth	9.8	5.3	5.3	6.3	7.0	6.3	6.3	6.0
GDP deflator	2.8	10.5	14.3	16.7	4.7	4.9	4.9	4.9
Consumer price index (period average)	-1.7	10.1	13.8	16.1	4.8	5.0	5.0	5.0
Consumer price index (end of period)	-0.8	14.9	27.0	7.0	4.8	5.0	5.0	5.0
External sector								
Export, f.o.b	79.4	-2.4	-3.9	7.0	3.3	7.7	7.2	7.1
Imports, c.i.f.	73.7	8.5	17.7	5.6	2.0	4.3	4.4	4.9
Export volume	64.0	-1.2	-10.6	42.2	1.5	4.5	4.9	4.6
Import volume	74.7	-5.3	7.3	-3.6	3.8	5.6	5.5	5.7
Terms of trade (deterioration -) [3]	10.0	-13.9	-2.0	-31.2	3.6	4.4	3.3	3.2
Public finance								
Revenue (excluding grants)	45.4	35.0	40.6	24.3	16.7	15.6	14.7	14.3
Total expenditure	40.6	37.9	54.4	5.9	11.4	10.8	7.0	10.4
Current expenditure	24.1	18.6	33.1	9.5	7.0	13.7	10.6	13.3
Investment expenditure and net lending	72.7	64.7	84.2	2.3	16.1	7.9	3.3	7.2
Money and credit [4]								
Broad money	8.2	12.6	23.0	19.2	15.0	14.5	14.5	14.5
Net foreign assets	14.9	59.3	78.7	13.6	16.9	19.0	19.9	23.6
Net domestic assets	5.7	-6.6	0.1	23.3	13.8	11.4	10.5	7.2
Credit to government [5]	13.7	-34.7	-34.4	-1.6	-2.2	1.2	0.9	-0.7
Credit to the private sector	22.2	22.2	36.9	22.8	20.3	20.7	20.4	20.0
Velocity of money (M3; average)	4.0	4.1	3.9	4.0	3.9	3.8	3.7	3.6
TB weighted-average auction rates								
(in percent; end of period)	10.8	...	17.4	...	...	...	...	...
	(In percent of GDP)							
Public finance								
Total revenue (excluding grants)	10.3	12.0	12.0	12.1	12.6	13.0	13.4	13.8
Of which : tax revenue	10.0	11.2	10.9	11.4	12.1	12.6	13.0	13.4
Total grants	5.1	7.9	8.2	5.5	5.5	5.2	5.0	4.8
Capital expenditure	7.8	11.5	12.5	10.3	10.7	10.3	9.6	9.2
Total expenditure	19.5	23.1	25.1	21.4	21.3	21.2	20.3	20.2
Overall balance (commitment basis, incl. grants)	-4.2	-3.4	-4.9	-3.9	-3.2	-2.9	-1.9	-1.6
Overall balance (commitment basis, excl. grants)	-9.3	-11.3	-13.1	-9.3	-8.7	-8.1	-6.9	-6.4
Domestic financing	1.8	-1.1	-1.0	0.3	-0.1	0.1	0.1	0.0

Table 1. Madagascar: Selected Economic and Financial Indicators, 2000-09 (concluded) [1/]

	2003	2004		2005	2006	2007	2008	2009
		Prog. [2]	Est.	Revised Projections				
	(In percent of GDP)							
Money and credit [4]								
Broad money	25.1	24.3	25.7	24.7	25.4	26.0	26.7	27.5
Net foreign assets	7.3	10.0	10.9	10.0	10.4	11.1	11.9	13.2
Net domestic assets	17.8	14.3	14.8	14.8	15.0	15.0	14.8	14.3
Credit to government [5]	9.1	5.1	5.0	3.9	3.4	3.1	2.8	2.5
Credit to the private sector	8.8	9.2	10.0	9.9	10.6	11.5	12.4	13.4
Savings and investment								
Resource gap	-9.0	-15.2	-16.3	-13.2	-11.4	-10.2	-8.8	-8.0
Investment	17.9	23.7	27.5	24.3	24.2	23.7	22.9	22.5
Government	7.8	11.5	12.5	10.3	10.7	10.3	9.6	9.2
Nongovernment	10.1	12.2	15.0	14.0	13.5	13.4	13.3	13.3
Gross domestic savings	8.9	8.6	11.1	11.1	12.7	13.6	14.1	14.6
Gross national savings	13.0	14.6	16.9	15.5	17.3	17.9	18.2	18.6
Public	-13.1	8.1	-5.0	-8.3	-9.0	-8.4	-7.6	-7.1
Private	26.1	6.4	21.8	23.8	26.3	26.3	25.8	25.7
External sector, public debt, and debt service								
Export, f.o.b	17.2	19.7	22.0	21.6	20.4	20.3	20.1	19.9
Imports, c.i.f.	24.3	33.5	38.1	36.8	34.5	33.1	31.9	31.0
Current account balance (excluding grants)	-7.5	-13.2	-14.4	-11.3	-9.4	-8.1	-6.8	-6.0
Current account balance (including grants)	-4.9	-9.2	-10.6	-8.8	-6.9	-5.8	-4.7	-4.0
Net present value (NPV) of external debt (after enhanced HIPC debt relief)								
NPV of debt-to-GDP ratio	61.7	53.3	52.1	48.7	47.2	45.5	43.4	41.4
NPV of debt-to-exports ratio [6]	305.7	213.5	202.1	169.8	161.4	153.4	147.4	141.1
	(In units indicated)							
Gross official reserves (in millions of SDRs)	284.4	327.5	333.5	335.1	373.8	428.2	491.6	573.4
In months of imports of goods and nonfactor services	2.7	3.0	2.8	2.7	3.0	3.2	3.5	3.9
Exchange rate: Ariary per SDR (period average)	1,734.8	...	2,772.1	...	...	...	...	...
Exchange rate: Ariary per U.S. dollar (period average)	1,240.6	...	1,870.8	...	...	...	...	...
GDP per capita (in U.S. dollars)	324	255	251	276	292	307	324	340
Nominal GDP (billions of Ariary)	6,778.6	7,889.1	8,155.7	10,114.5	11,331.8	12,638.1	14,094.8	15,675.1

Sources: Malagasy authorities; and Fund staff estimates and projections.

[1] Data may not add up due to rounding.

[2] IMF Country Report No. 04/404, December 10, 2004.

[3] Based on 1993 trade weights.

[4] The composition of monetary growth in 2003 reflects reclassification of a public enterprise, SOLIMA, debt (FMG 350.4 billion) by the government.

[5] For 2003, include the takeover of SOLIMA debt by the government.

[6] Based on the average of three consecutive years of exports of goods and services ending in the current year. (e.g., export average over 2001-2003 for NPV of debt-to-exports ratio in 2003).

Table 2. Madagascar: Central Government Accounts, 2003-09
(In billions of Ariary)

	2003	2004		2005	2006	2007	2008	2009
		Prog. 1/	Est.	Revised Projections				
Total revenue and grants	1,045.0	1,565.4	1,653.4	1,774.6	2,046.6	2,310.3	2,592.7	2,915.5
Total revenue	698.9	943.5	982.3	1,220.9	1,424.6	1,647.5	1,889.2	2,159.5
Budgetary revenue	698.9	943.5	982.3	1,220.9	1,424.6	1,647.5	1,889.2	2,159.5
Tax revenue	678.5	883.6	887.1	1,151.3	1,371.2	1,592.4	1,832.3	2,100.5
Nontax revenue	20.4	59.9	95.2	69.5	53.5	55.1	56.9	59.0
Grants	346.1	621.9	671.1	553.8	622.0	662.8	703.5	756.0
Current grants	171.9	290.0	318.7	205.5	245.1	255.7	263.8	282.0
Of which: HIPC assistance	38.3	36.2	62.2	55.5	87.1	86.0	81.5	86.8
Project grants	174.2	331.9	352.4	348.2	376.9	407.1	439.8	474.0
Total expenditure	1,324.4	1,826.1	2,045.3	2,166.4	2,413.0	2,674.0	2,861.2	3,159.7
Current expenditure	771.7	915.4	1,027.3	1,124.9	1,203.8	1,369.1	1,513.7	1,715.4
Budgetary expenditure	751.6	882.2	896.9	1,054.0	1,153.2	1,324.5	1,475.1	1,682.8
Personnel	365.4	386.3	400.0	457.6	543.9	624.3	683.6	772.8
Of which: HIPC financed	24.0	23.9	...	...	...	...	...	...
Other noninterest expenditure	236.1	255.4	257.4	316.5	394.2	482.6	572.1	689.5
Of which: HIPC financed	23.9	20.4	...	...	...	...	...	...
Foreign interest obligations	60.6	112.1	113.9	139.5	133.8	140.3	146.3	152.3
Domestic interest obligations	89.5	128.4	125.5	140.5	81.3	77.2	73.2	68.2
Treasury operations (net) [2]	12.1	32.1	128.6	69.1	50.0	44.0	38.0	32.0
Emergency expenditure	7.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Counterpart-funds-financed operations	0.9	1.2	1.8	1.8	0.6	0.6	0.6	0.6
Capital expenditure	531.5	910.6	1,018.0	1,041.5	1,209.3	1,304.9	1,347.5	1,444.3
Domestically financed	172.3	240.0	229.5	273.8	407.9	497.9	555.3	617.6
Foreign financed	359.2	670.6	788.5	767.7	801.3	807.0	792.2	826.7
Of which : HIPC financed	24.7	19.0	...	...	...	...	...	...
Government on-lending	21.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Primary balance [3]	77.3	233.8	175.1	361.3	416.4	478.8	580.3	652.6
Overall balance (commitment basis, excluding the cost of structural reforms)								
Including grants	-279.5	-260.7	-391.8	-391.8	-366.4	-363.7	-268.5	-244.1
Excluding grants	-625.5	-882.6	-1,062.9	-945.5	-988.4	-1,026.5	-972.0	-1,000.2
Net cost of structural reforms [4]	-3.9	-8.5	-8.8	1.8	0.0	0.0	0.0	0.0
Exceptional revenue	1.2	1.5	1.2	1.8	0.0	0.0	0.0	0.0
Cost of structural reforms	5.1	10.0	10.0	0.0	0.0	0.0	0.0	0.0
Overall balance (commitment basis, including the cost of structural reforms)								
Excluding grants	-629.5	-269.3	-1,071.7	-943.7	-988.4	-1,026.5	-972.0	-1,000.2
Including grants	-283.4	-891.2	-400.6	-390.0	-366.4	-363.7	-268.5	-244.1
Domestic balance [5]	-209.7	-108.4	-169.3	-36.5	-53.3	-79.2	-33.6	-21.2
Change in arrears	-41.0	-69.5	-63.2	-45.6	-53.2	-43.2	-43.2	-43.2
Total overall balance (cash basis, excluding gran	-670.5	-960.6	-1,134.9	-989.3	-1,041.6	-1,069.7	-1,015.2	-1,043.3
Total overall balance (cash basis, including grant	-324.4	-338.7	-463.8	-435.6	-419.6	-406.9	-311.6	-287.3

Table 2. Madagascar: Central Government Accounts, 2003-09 (concluded)
(In billions of Ariary)

	2003	2004 Prog. 1/	2004 Est.	2005	2006	2007	2008	2009
				Revised Projections				
Financing	324.4	338.7	463.8	435.6	419.6	406.9	311.6	287.3
Foreign (net)	191.6	401.2	518.2	406.7	435.6	396.4	303.0	291.7
Drawings	249.3	456.6	579.3	489.1	554.0	533.1	455.2	458.4
Budget	64.3	136.8	143.2	121.9	129.6	133.3	102.8	105.7
Projects	185.0	319.7	436.1	367.1	424.4	399.8	352.4	352.7
Amortization due	-126.9	-145.4	-188.5	-193.3	-194.8	-180.8	-200.4	-218.6
Change in external arrears	-13.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0
External debt relief [6]	82.6	90.0	127.4	111.0	76.3	44.1	48.2	51.9
Domestic (net)	119.3	-89.7	-84.6	27.1	-16.0	10.5	8.7	-4.4
Banking system [7]	8.8	-202.7	-215.6	-3.5	-8.0	5.2	4.3	-2.2
Nonbanking system	84.5	95.6	107.9	30.6	-8.0	5.2	4.3	-2.2
Treasury correspondent accounts (net)	26.0	17.4	23.0	0.0	0.0	0.0	0.0	0.0
Privatization receipts	13.5	27.2	30.2	1.8	0.0	0.0	0.0	0.0

Sources: Ministry of Economy, Finance, and Budget; and Fund staff estimates and projections.

[1] IMF Country Report No. 04/404, December 10, 2004.
[2] Includes annexed budgets of quasi-public entities, including port authorities, the post office, government printing office, civil service retirement funds, and correspondent accounts of local authorities.
[3] Defined as total revenue (excluding non-tax revenues from the central bank) minus current expenditure (excluding domestic and foreign interest payments).
[4] The net cost of structural reforms comprises (a) as receipts, loan recovery by the debt-recovery unit that holds the nonperforming loans of the two (former) public banks (BFV and BTM) after the financial restructuring of their assets; and (b) as expenditures, those related to civil service reform (i.e., training, bonuses, and wage decompression); to the upgrading of pay and equipment in the justice services; to privatization (severance pay, administrative costs, transfers to the regional development fund that provides grants and concessional loans for basic social infrastructure purposes or to employees affected by privatization, and indemnization payments to formerly expropriated owners); and to the capital transfers for the asset restructuring at the two insolvent banks (BFV and BTM).
[5] Total revenue minus expenditure, excluding foreign interest payments and foreign-financed capital expenditure.
[6] HIPC bilateral relief.
[7] Excludes the effect of exchange rate changes on net credit to government in foreign exchange.

Table 3. Madagascar: Central Government Accounts, 2003-09
(In percent of GDP, unless otherwise indicated)

	2003	2004		2005	2006	2007	2008	2009
		Prog. 1/	Est.	Revised Projections				
Total revenue and grants	15.4	19.8	20.3	17.5	18.1	18.3	18.4	18.6
Total revenue	10.3	12.0	12.0	12.1	12.6	13.0	13.4	13.8
Tax revenue	10.0	11.0	10.9	11.4	12.1	12.6	13.0	13.4
Nontax revenue	0.3	0.8	1.2	0.7	0.5	0.4	0.4	0.4
Grants	5.1	7.9	8.2	5.5	5.5	5.2	5.0	4.8
Current grants	2.5	3.7	3.9	2.0	2.2	2.0	1.9	1.8
Of which: HIPC assistance	0.6	0.5	0.8	0.5	0.8	0.7	0.6	0.6
Project grants	2.6	4.2	4.3	3.4	3.3	3.2	3.1	3.0
Total expenditures	19.5	23.1	25.1	21.4	21.3	21.2	20.3	20.2
Current expenditure	11.4	11.6	12.6	11.1	10.6	10.8	10.7	10.9
Noninterest expenditure	8.9	8.1	8.1	7.7	8.3	8.8	8.9	9.3
Personnel	5.4	4.9	4.9	4.5	4.8	4.9	4.9	4.9
Of which: HIPC financed	0.4	0.3	...	...	...	...	...	...
Other noninterest expenditure	3.5	3.2	3.2	3.1	3.5	3.8	4.1	4.4
Of which: HIPC financed	0.4	0.3	...	...	...	...	...	...
Interest obligations	2.2	3.0	2.9	2.8	1.9	1.7	1.6	1.4
Treasury operations [2]	0.2	0.4	1.6	0.7	0.4	0.3	0.3	0.2
Emergency expenditures	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Capital expenditure	7.8	11.5	12.5	10.3	10.7	10.3	9.6	9.2
Domestically financed expenditure	2.5	3.0	2.8	2.7	3.6	3.9	3.9	3.9
Foreign-financed expenditure	5.3	8.5	9.7	7.6	7.1	6.4	5.6	5.3
Of which : HIPC financed	0.4	0.2	...	...	...	...	...	...
Government on-lending	0.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic budgetary balance	-2.7	-1.3	-2.0	-0.4	-0.5	-0.6	-0.2	-0.1
Primary balance [3]	1.1	3.0	2.1	3.6	3.7	3.8	4.1	4.2
Net cost of structural reforms [4]	-0.1	-0.1	-0.1	0.0	0.0	0.0	0.0	0.0
Exceptional revenue	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Cost of structural reforms	0.1	0.1	0.1	0.0	0.0	0.0	0.0	0.0
Overall balance (commitment basis)								
Excluding grants	-9.3	-11.3	-13.1	-9.3	-8.7	-8.1	-6.9	-6.4
Including grants	-4.2	-3.4	-4.9	-3.9	-3.2	-2.9	-1.9	-1.6
Domestic balance [5]	-3.1	-1.4	-2.1	-0.4	-0.5	-0.6	-0.2	-0.1
Change in arrears	-0.6	-0.9	-0.8	-0.5	-0.5	-0.3	-0.3	-0.3
Total overall balance (cash basis, excluding grants)	-9.9	-12.2	-13.9	-9.8	-9.2	-8.5	-7.2	-6.7
Total overall balance (cash basis, including grants)	-4.8	-4.3	-5.7	-4.3	-3.7	-3.2	-2.2	-1.8

Table 3. Madagascar: Central Government Accounts, 2003-09 (concluded)
(In percent of GDP, unless otherwise indicated)

	2003	2004		2005	2006	2007	2008	2009
		Prog. 1/	Est.	Revised Projections				
Financing	4.8	4.3	5.7	4.3	3.7	3.2	2.2	1.8
Foreign (net)	2.8	5.1	6.4	4.0	3.8	3.1	2.1	1.9
Drawings	3.7	5.8	7.1	4.8	4.9	4.2	3.2	2.9
Budget	0.9	1.7	1.8	1.2	1.1	1.1	0.7	0.7
Projects	2.7	4.1	5.3	3.6	3.7	3.2	2.5	2.3
Amortization due	-1.9	-1.8	-2.3	-1.9	-1.7	-1.4	-1.4	-1.4
Change in external arrears	-0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0
External debt relief [6]	1.2	1.1	1.6	1.1	0.7	0.3	0.3	0.3
Domestic (net)	1.8	-1.1	-1.0	0.3	-0.1	0.1	0.1	0.0
Of which: banking system [7]	0.1	-2.6	-2.6	0.0	-0.1	0.0	0.0	0.0
Privatization receipts	0.2	0.3	0.4	0.0	0.0	0.0	0.0	0.0
Memorandum items:								
Nominal GDP (in billions of Ariary)	6,779	7,889	8,156	10,114	11,332	12,638	14,095	15,675
Total domestic debt	16.0	12.3	11.5	9.2	7.8	6.6	5.6	4.7

Sources: Ministry of Economy, Finance, and Budget; and Fund staff estimates and projections.

[1] IMF Country Report No. 04/404, December 10, 2004.
[2] Includes annexed budgets of quasi-public entities, including port authorities, the post office, government printing office, civil service retirement funds, and correspondent accounts of local authorities.
[3] Defined as total revenue (excluding non-tax revenues from the central bank) minus current expenditure (excluding domestic and foreign interest payments).
[4] The net cost of structural reforms comprises (a) as receipts, loan recovery by the debt-recovery unit that holds the nonperforming loans of the two (former) public banks (BFV and BTM) after the financial restructuring of their assets; and (b) as expenditures, those related to civil service reform (i.e., training, bonuses, and wage decompression); to the upgrading of pay and equipment in the justice services; to privatization (severance pay, administrative costs, transfers to the regional development fund that provides grants and concessional loans for basic social infrastructure purposes or to employees affected by privatization, and indemnization payments to formerly expropriated owners); and to the capital transfers for the asset restructuring at the two insolvent banks (BFV and BTM).
[5] Total revenue minus expenditure, excluding foreign interest payments and foreign-financed capital expenditure.
[6] HIPC bilateral relief.
[7] Excludes the effect of exchange rate changes on net credit to government in foreign exchange.

Table 4. Madagascar: Monetary Survey, 2003-05
(In billions of Ariary, unless otherwise indicated)

	2003	2004					2005			
	Dec.	Mar.	Jun.	Sep.	Dec.		Mar.	Jun.	Sep.	Dec.
					Prog. 1/	Act.	Proj.	Proj.	Proj.	Proj.
Net foreign assets	495.9	755.2	778.4	951.2	789.8	886.2	1,010.1	1,005.6	1,008.0	1,007.3
Net foreign assets (BCM)	284.8	467.4	437.4	608.6	468.5	513.4	586.3	581.8	584.3	583.5
Net foreign assets (domestic money banks)	211.1	287.8	341.0	342.6	321.2	372.8	423.8	423.8	423.8	423.8
Net domestic assets	1,208.7	1,081.6	1,140.8	1,020.6	1,129.1	1,209.9	1,232.8	1,279.2	1,402.5	1,491.3
Domestic credit	1,301.9	1,294.1	1,369.1	1,251.5	1,227.4	1,331.6	1,376.4	1,443.8	1,396.9	1,510.8
Net credit to government (budget)	615.7	592.4	568.7	406.0	402.3	403.8	374.0	415.0	338.8	397.4
Other claims on public sector	82.1	84.8	86.0	90.1	85.0	93.2	93.2	93.2	93.2	93.2
Credit to the economy	604.1	616.9	714.4	755.3	740.1	834.6	909.3	935.7	964.9	1,020.3
Credit to public enterprises	9.2	11.8	13.7	13.2	13.2	19.9	19.9	19.9	19.9	19.9
Credit to private sector	594.9	605.1	700.8	742.1	726.9	814.7	889.3	915.7	945.0	1,000.3
Other items (net; asset +)	-93.2	-212.5	-228.2	-230.9	-98.3	-121.7	-143.6	-164.6	5.6	-19.6
M3	1,704.6	1,836.8	1,919.2	1,971.8	1,918.9	2,096.1	2,242.9	2,284.8	2,410.6	2,498.6
Foreign currency deposits	217.4	311.4	347.0	357.6	315.7	349.3	388.9	388.9	388.9	397.1
M2	1,487.2	1,525.4	1,572.2	1,614.2	1,603.2	1,746.8	1,853.9	1,895.9	2,021.6	2,101.5
Currency in circulation	514.0	477.9	529.8	545.1	518.1	579.0	605.6	616.9	650.9	674.6
Deposits in local currency	937.7	1,014.8	1,009.8	1,043.1	1,052.6	1,139.5	1,220.0	1,250.6	1,342.4	1,398.6
Short-term obligations of commercial banks	35.4	32.7	32.6	26.0	32.5	28.4	28.4	28.4	28.4	28.4
Memorandum items:	(Percent change since the end of the previous year, unless otherwise indicated)									
M3	8.2	7.8	12.6	15.7	12.6	23.0	7.0	9.0	15.0	19.2
M2	6.3	2.6	5.7	8.5	7.8	17.5	6.1	8.5	15.7	20.3
Domestic credit	9.4	-0.6	5.2	-3.9	-5.7	2.3	3.4	8.4	4.9	13.5
Credit to the private sector	22.2	1.7	17.8	24.8	22.2	36.9	9.2	12.4	16.0	22.8
Net credit to government	13.7	-3.8	-7.6	-34.1	-34.7	-34.4	-7.4	2.8	-16.1	-1.6
Reserve money	-0.3	1.5	-3.9	-0.9	-1.4	17.4	5.6	7.5	13.1	17.1
Currency/M3 (in percent)	30.2	26.0	27.6	27.6	27.0	27.6	27.0	27.0	27.0	27.0
Reserve money multiplier (M3/reserves)	2.4	2.6	2.8	2.8	2.8	2.5	2.6	2.6	2.6	2.6
Velocity of money (GDP/end-of-period M3)	4.0	...	...	...	4.1	3.9	...	...	...	4.0
Exchange rate (Ariary per SDR; end of period) 2/	1,805.4	2,616.0	3,033.3	3,046.7	2,747.9	2,895.7	3,291.4	3,291.4	3,291.4	3,291.4

Sources: Central Bank of Madagascar (BCM); and Fund staff estimates and projections.

1/ IMF Country Report, No. 04/404, December 10, 2004.
2/ Exchange rate for monetary programming purposes.

Table 5. Madagascar: Balance Sheet of the Central Bank (BCM), 2003-05
(In billions of Ariary, unless otherwise indicated)

	2003	2004					2005				
		Mar.	Jun.	Sep.	Dec.		Mar.		Jun.	Sep.	Dec.
					Prog. 1/	Act.	Proj.	Act.	Proj.	Proj.	Proj.
Net foreign assets	284.8	467.4	437.4	608.6	468.5	513.4	586.3	477.4	581.8	584.3	583.5
Net domestic assets	420.1	247.8	240.0	89.9	226.5	313.9	287.4	316.9	307.4	351.4	384.9
Overall credit to government (net)	339.5	262.4	290.6	201.2	243.9	262.9	255.0	271.9	296.0	219.9	278.5
Liquidity operations 2/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net credit to government (budget)	339.5	262.4	290.6	201.2	243.9	262.9	255.0	271.9	296.0	219.9	278.5
Claims on public enterprises	3.5	3.6	3.9	3.9	3.6	3.9	3.9	4.0	3.9	3.9	3.9
Credit to banks	3.4	3.3	2.7	-68.5	3.1	-7.7	-7.7	-22.9	-7.7	-7.7	-7.7
Other items (net; asset +)	73.7	-21.5	-57.2	-46.7	-24.1	54.8	36.2	63.9	15.2	135.4	110.2
Of which : valuation account (losses -)	-1.4	-113.7	-167.3	-170.2	-151.1	-104.7	-175.9	-105.3	-175.9	-175.9	-175.9
Reserve money	704.9	715.2	677.4	698.5	695.0	827.3	873.7	794.3	889.2	935.7	968.4
Currency outside banks	514.0	477.9	529.8	545.1	518.1	579.0	605.6	535.7	616.9	650.9	674.6
Bank reserves	190.9	237.3	147.6	153.4	176.9	248.4	268.1	258.6	272.3	284.9	293.8
Currency in banks	30.2	28.5	33.5	34.1	35.2	40.2	43.0	37.8	43.0	43.0	43.0
Deposits	160.8	208.8	114.2	119.3	141.8	208.2	225.1	220.8	229.3	241.9	250.8

Sources: Central Bank of Madagascar (BCM); and Fund staff estimates and projections.

1/ IMF Country Report, No. 04/404, December 10, 2004.
2/ Sales of treasury bills for monetary policy purposes.

Table 7. Madagascar: Balance of Payments, 2003-09
(In millions of SDRs, unless otherwise indicated)

	2003	2004		2005	2006	2007	2008	2009
		Prog. 1/	Est.	Revised Projections				
Current account	-191.8	-277.6	-311.3	-283.4	-241.7	-220.3	-192.2	-175.8
Goods and services	-351.1	-458.7	-480.5	-423.7	-399.6	-385.2	-362.1	-354.0
Trade balance	-135.9	-284.2	-303.2	-312.5	-310.3	-299.3	-291.2	-286.9
Exports	672.8	596.4	646.4	692.0	714.6	769.3	824.9	883.5
Imports	-808.7	-880.6	-949.6	-1004.4	-1,024.9	-1,068.6	-1,116.1	-1,170
Net services (net)	-215.2	-174.5	-177.3	-111.2	-89.3	-85.9	-70.9	-67.0
Services, receipts	229.3	256.7	285.3	357.5	405.8	437.6	482.8	518.8
Services, payments	-444.5	-431.2	-462.6	-468.6	-495.2	-523.4	-553.7	-585.9
Income (net)	-57.0	-48.6	-53.5	-57.4	-53.0	-54.6	-56.5	-58.2
Receipts	11.7	22.0	10.0	10.6	11.3	11.9	12.2	12.6
Payments	-68.7	-70.6	-63.5	-68.0	-64.2	-66.5	-68.7	-70.8
Of which : government interest [2]	-40.5	-40.9	-40.6	-44.3	-41.3	-42.1	-42.7	-43.2
Current transfers	216.4	229.7	222.7	197.7	210.9	219.5	226.4	236.4
Government	102.0	119.7	112.8	80.1	85.6	86.7	87.0	90.0
Budget aid	91.6	109.3	99.1	64.1	75.6	76.7	77.0	80.0
HIPC relief [3]	22.2	20.3	22.4	17.6	26.9	25.8	23.8	24.6
Grants	69.5	89.0	76.7	46.5	48.8	50.9	53.2	55.4
Other (net) [4]	10.4	10.4	13.7	16.0	10.0	10.0	10.0	10.0
Private	114.4	110.0	109.9	117.6	125.2	132.8	139.4	146.4
Capital and financial account	165.3	250.4	287.1	247.6	274.7	279.8	259.4	265.3
Capital account (government project grant	63.8	124.5	122.0	110.5	116.3	122.2	128.3	134.5
Financial account	28.9	125.9	144.2	137.0	158.3	157.6	131.0	130.8
Direct investment	9.1	30.0	30.0	48.2	52.5	56.9	61.7	66.7
Of which : privatization receipts	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	19.8	95.9	114.2	88.9	105.9	100.7	69.3	64.1
Government	47.6	105.6	135.7	93.9	110.9	105.7	74.3	69.1
Drawing	121.0	173.6	203.9	155.2	171.0	160.0	132.8	131.1
Project drawings	83.5	122.9	153.7	116.5	131.0	120.0	102.8	100.1
Budgetary support	37.5	50.7	50.2	38.7	40.0	40.0	30.0	30.0
Non-government	0.0	0.0	0.0	0.0	0.0	0.0	0.0	1.0
Amortization [2]	-73.4	-68.0	-68.2	-61.4	-60.1	-54.3	-58.5	-62.0
Private sector amortization	-7.0	-9.7	-9.7	-5.0	-5.0	-5.0	-5.0	-5.0
Banks, net	-20.8	0.0	-11.8	0.0	0.0	0.0	0.0	0.0
Other (incl. errors and omissions) [5]	72.6	0.0	21.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-26.4	-27.2	-24.2	-35.8	32.9	59.5	67.2	89.5

Table 7. Madagascar: Balance of Payments, 2003-09 (concluded)
(In millions of SDRs, unless otherwise indicated)

	2003	2004		2005	2006	2007	2008	2009
		Prog. 1/	Proj.	Revised Projections				
Financing	26.4	27.2	24.2	35.8	-32.9	-59.5	-67.2	-89.5
Net foreign assets (increase -)	-11.9	-13.4	-19.6	0.7	-56.5	-72.7	-81.2	-104.2
Use of Fund credit (net)	5.9	29.5	29.5	2.3	-17.8	-18.4	-17.8	-22.4
Disbursements	11.3	34.9	34.9	11.3	0.0	0.0	0.0	0.0
Repayments	-5.4	-5.4	-5.4	-9.1	-17.8	-18.4	-17.8	-22.4
Other assets, net (increase -)	-17.8	-42.9	-49.1	-1.6	-38.7	-54.4	-63.4	-81.8
Debt relief and cancellation 6/	47.8	40.6	43.7	35.1	23.6	13.2	14.1	14.7
Memorandum items:								
Grants (in percent of GDP)	4.2	8.1	8.0	5.9	5.8	5.5	5.2	5.0
Loans (in percent of GDP)	1.2	3.5	4.6	2.9	3.2	2.8	1.8	1.6
Direct investment (in percent of GDP)	0.2	1.0	1.0	1.5	1.5	1.5	1.5	1.5
Current account (in percent of GDP)								
Excluding net official transfers	-7.5	-13.2	-14.4	-11.3	-9.4	-8.1	-6.8	-6.0
Including net official transfers	-4.9	-9.2	-10.6	-8.8	-6.9	-5.8	-4.7	-4.0
Gross official reserves	284.4	327.5	333.5	335.1	373.8	428.2	491.6	573.4
(in months of imports of goods and nonfactor servic	2.7	3.0	2.8	2.7	3.0	3.2	3.5	3.9
Exchange rates								
Ariary/SDR (period average)	1,734.8	...	2,772.1	...	...	...	...	...
Ariary/U.S. dollar (period average)	1,240.6	...	1,870.8	...	...	...	...	...

Sources: Central Bank of Madagascar, Ministry of Finance, IMF Finance Dept., and Fund staff estimates and projections.

[1] IMF Country Report No. 04/404, December 10, 2004..

[2] Interest and amortization payments are based on the HIPC completion point document www.imf.org and authorities' estimates.

[3] HIPC relief provided by multilateral creditors including the African Development Bank Group (AfDB), IDA, and the IMF.

[4] Other official grants less payments due to scholarships and contributions to international organizations.

[5] Includes commercial credits received or granted.

[6] HIPC bilateral debt relief.

Table 8. Madagascar: Sources and Uses of Resources, 2003-09

	2003	2004		2005	2006	2007	2008	2009
	Est.	Prog. 1/	Proj.	Projections				
	(In billions of Ariary)							
GDP	6,778.6	7,889.1	8,155.7	10,114.5	11,331.8	12,638.1	14,094.8	15,675.1
Consumption	6,174.8	7,213.5	7,248.8	8,992.0	9,887.6	10,923.0	12,113.6	13,393.4
Public	621.6	674.9	748.4	845.0	521.9	582.3	642.5	717.4
Private	5,553.2	6,538.6	6,500.5	8,147.0	9,365.8	10,340.7	11,471.0	12,676.0
Investment	1,212.9	1,873.4	2,238.9	2,457.5	2,739.1	2,998.4	3,222.1	3,529.1
Domestic investment	1,212.9	1,873.4	2,238.9	2,457.5	2,739.1	2,998.4	3,222.1	3,529.1
Government	531.5	910.6	1,018.0	1,041.5	1,209.3	1,304.9	1,347.5	1,444.3
Private	681.4	962.8	1,220.9	1,416.0	1,529.8	1,693.5	1,874.6	2,084.8
Of which: direct foreign investmen	15.8	78.3	83.2	151.7	170.0	189.6	211.4	235.1
Changes in stocks	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Resource gap	-609.1	-1,197.8	-1,332.0	-1,335.0	-1,294.8	-1,283.3	-1,240.9	-1,247.4
Exports of goods and nonfactor services	1,564.9	2,227.5	2,582.8	3,306.6	3,630.2	4,021.4	4,480.9	4,941.7
Of which : exports of goods	1,167.1	1,557.2	1,792.0	2,180.3	2,315.4	2,563.4	2,826.6	3,113.3
Imports of goods and nonfactor services	2,174.0	3,425.4	3,914.8	4,641.6	4,925.1	5,304.7	5,721.7	6,189.0
Of which : imports of goods	1,402.9	2,299.4	2,632.5	3,164.9	3,320.8	3,560.6	3,824.4	4,124.4

Table 8. Madagascar: Sources and Uses of Resources, 2003-09 (concluded)

	2003	2004		2005		2006	2007	2008	2009
	Est.	Prog. 1/	Proj.	Proj. 2/	Rev. Proj.	Projections			
	(In percent of GDP)								
Consumption	91.1	91.4	88.9	88.3	88.9	87.3	86.4	85.9	85.4
Public	9.2	8.6	9.2	8.1	8.4	4.6	4.6	4.6	4.6
Private	81.9	82.9	79.7	80.2	80.5	82.6	81.8	81.4	80.9
Investment	17.9	23.7	27.5	24.9	24.3	24.2	23.7	22.9	22.5
Domestic investment	17.9	23.7	27.5	24.9	24.3	24.2	23.7	22.9	22.5
Government	7.8	11.5	12.5	10.9	10.3	10.7	10.3	9.6	9.2
Private	10.1	12.2	15.0	14.0	14.0	13.5	13.4	13.3	13.3
Of which: direct foreign investmen	0.2	1.0	1.0	1.5	1.5	1.5	1.5	1.5	1.5
Changes in stocks	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Resource gap	-9.0	-15.2	-16.3	-13.3	-13.2	-11.4	-10.2	-8.8	-8.0
Exports of goods and nonfactor services	23.1	28.2	31.7	29.9	32.7	32.0	31.8	31.8	31.5
Of which : exports of goods	17.2	19.7	22.0	21.0	21.6	20.4	20.3	20.1	19.9
Imports of goods and nonfactor services	32.1	43.4	48.0	43.2	45.9	43.5	42.0	40.6	39.5
Of which : imports of goods	20.7	29.1	32.3	29.5	31.3	29.3	28.2	27.1	26.3
Gross domestic savings	8.9	8.6	11.1	11.7	11.1	12.7	13.6	14.1	14.6
Government	5.7	3.0	12.8	3.9	17.9	-10.6	-10.1	-9.5	-9.2
Nongovernment	3.2	5.6	-1.7	7.8	-6.8	23.4	23.7	23.5	23.7
Current account									
Excluding grants	-7.5	-13.2	-14.4	-10.8	-11.3	-9.4	-8.1	-6.8	-6.0
Including grants	-4.9	-9.2	-10.6	-8.2	-8.8	-6.9	-5.8	-4.7	-4.0
Gross national savings	13.0	14.6	16.9	16.8	15.5	17.3	17.9	18.2	18.6
Government 3/	-13.1	8.1	-5.0	7.6	-8.3	-9.0	-8.4	-7.6	-7.1
Nongovernment	26.1	6.4	21.8	9.2	23.8	26.3	26.3	25.8	25.7

Sources: Ministry of Economy, Finance, and Budget; and Fund staff estimates and projections.

1/ IMF Country Report No. 04/404, December 10, 2004.
3/ Defined as overall fiscal balance (on commitment bases, after net cost of restructuring) plus public investment expenditure.

Table 9: Madagascar: Millennium Development Goals

	1990	1995	2001	2002	2015 Target
Goal 1. Eradicate extreme poverty and hunger					
Target 1: Halve between 1990 and 2015, the proportion of people whose income is less than one dollar a day.					
1. Population below US$ 1 a day (percent)	...	...	49.1	...	
2. Poverty gap ratio at US$ 1 a day (percent)	...	...	18.3	...	
3. Share of income or consumption held by poorest 20 percent (percent)	...	...	6.4	...	
Target 2: Halve, between 1990 and 2015, the proportion of people suffering hunger					
4. Prevalence of child malnutrition (percent of children under 5)	40.9	34.1	...	33.1	20.5
5. Population below minimum level of dietary energy consumption (percent)	35.0	40.0	36.0	...	17.5
Goal 2. Achieve universal primary education					
Target 3: Ensure that, by 2015, children will be able to complete a full course of primary schooling					
6. Net primary enrollment ratio (percent of relevant age group)	...	60.6	68.7	...	
7. Percentage of cohort reaching grade 5	21.5	39.7	33.6	...	
8. Youth literacy rate (percent age 15-24)	72.2	76.3	80.8	81.5	
Goal 3. Promote gender equality and empower women					
Target 4: Eliminate gender disparity in primary and secondary education preferably by 2005 and to all levels of education by 2015					
9. Ratio of girls to boys in primary and secondary education (percent)	98.9	99.2	...	...	100.0
10. Ratio of young literate females to males (percent ages 15-24)	85.6	88.8	92.1	92.5	
11. Share of women employed in the nonagricultural sector (percent)	26.0	...	...	...	
12. Proportion of seats held by women in the national parliament (percent)	7.0	4.0	8.0	8.0	

Table 9: Madagascar: Millennium Development Goals (continued)

	1990	1995	2001	2002	2015 Target
<u>Goal 4. Reduce child mortality</u>					
Target 5: reduce by two-thirds between 1990 and 2015, the under-five mortality rate					
13. Under-five mortality rate (per 1,000)	168.0	156.0	139.0	135.0	54.0
14. Infant mortality rate (per 1,000 live births)	103.0	95.0	86.0	84.0	
15. Immunization against measles (percent of children under 12-months)	47.0	55.0	55.0	61.0	
<u>Goal 5. Improve maternal health</u>					
Target 6: Reduce by three-quarters, between 1990 and 2015, the maternal mortality ratio.					
16. Maternal mortality ratio (modeled estimate, per 100,000 live births)	...	580.0	550.0	...	127.0
17. Proportion of births attended by skilled health personnel	57.0	47.3	46.2	...	
<u>Goal 6. Combat HIV/AIDS, malaria and other diseases</u>					
Target 7: Halt by 2015, and begin to reverse, the spread of HIV/AIDS					
18. HIV prevalence among females (percent ages 15-24)	...	...	0.2	...	
19. Contraceptive prevalence rate (percent of women ages 15-49)	16.7	19.4	...	16.9	
20. Number of children orphaned by HIV/AIDS	...	...	6,300	...	
Target 8: Halt by 2015, and begin to reverse, the incidence of malaria and other major diseases					
21. Prevalence of death associated with malaria	...	...	...	...	
22. Share of population in malaria risk areas using effective prevention and treatment	...	...	...	...	
23. Incidence of tuberculosis (per 100,000 people)	...	...	254.5	...	
24. Tuberculosis cases detected under DOTS (percent)	...	65.0	60.0	61.6	

Table 9: Madagascar: Millennium Development Goals (concluded)

	1990	1995	2001	2002	2015 Target
Goal 7. Ensure environmental sustainability					
Target 9: Integrate the principles of sustainable development into policies and programs. Reverse the loss of environmental resources					
25. Forest area (percent of total land area)	22.2	...	20.2	...	
26. Nationally protected areas (percent of total land area)	...	1.9	1.9	2.1	
27. GDP per unit of energy use (PPP $ per kg oil equivalent)	...	...	...	...	
28. CO2 emissions (metric tons per capita)	0.1	0.1	0.1	...	
29. Proportion of population using solid fuels					
Target 10: Halve by 2015 proportion of people without access to safe drinking water					
30. Access to improved water source (percent of population)	44.0	...	47.0	...	72.0
Target 11: Achieve by 2020 significant improvement for at least 100 million slum dwellers					
31. Access to improved sanitation (percent of population)	36.0	...	42.0	...	
32. Access to secure tenure (percent of population)	...	...	...	...	
Goal 8. Develop a Global Partnership for Development 1/					
Target 16: Develop and implement strategies for productive work for youth.					
45. Unemployment rate of population ages 15-24 (total)	...	...	...	...	
Female	...	...	...	...	
Male	...	...	...	...	
Target 17: Provide access to affordable essential drugs					
46. Proportion of population access with access to affordable essential drugs	...	...	...	...	
Target 18: Make available new technologies, especially information and communications					
47. Fixed line and mobile telephones (per 1,000 people)	2.8	3.0	13.3	14.0	...
48. Personal computers (per 1,000 people)		1.5	2.6	4.4	...

Sources: World Bank; and Fund staff estimates.

1/ Targets 12-15 and indicators 33-44 are excluded because they can not be measured on a country specific basis. These are related to official development assistance, market access, and the HIPC initiative.

Madagascar: Relations with the Fund
(As of March 31, 2005)

I. Membership Status: Joined 9/25/63; Article VIII

II. General Resources Account:

	SDR Millions	% Quota
Quota	122.20	100.00
Fund holdings of currency	122.17	99.98
Reserve position in Fund	0.03	0.02

III. SDR Department:

	SDR Millions	% Allocation
Net cumulative allocation	19.27	100.00
Holdings	0.01	0.06

IV. Outstanding Purchases and Loans:

	SDR Millions	% Quota
Poverty Reduction and Growth Facility (PRGF) arrangements	154.06	126.07

V. Financial Arrangements:

Type	Approval Date	Expiration Date	Amount Approved (SDR millions)	Amount Drawn (SDR millions)
PRGF	03/01/01	03/01/05	91.65	91.65
ESAF/PRGF	11/27/96	11/30/00	81.36	78.68
ESAF	05/15/89	05/14/92	76.90	51.27

VI. Projected Payments to Fund (without HIPC Initiative Assistance)
(SDR million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2005	2006	2007	2008	2009
Principal	5.42	16.87	17.56	17.12	21.75
Charge/interest	1.11	1.17	1.08	1.00	0.90
Total	6.53	18.04	18.65	18.12	22.65

Projected Payments to Fund (with Board-approved HIPC Initiative Assistance)
(SDR million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2005	2006	2007	2008	2009
Principal	4.64	11.66	14.25	17.12	21.75
Charges/interest	1.11	1.17	1.08	1.00	0.90
Total	5.74	12.84	15.33	18.12	22.65

VII. Implementation of HIPC Initiative:

Commitment of HIPC Initiative assistance	Enhanced framework
Decision point date	12/21/2000
Assistance committed (NPV terms)	
Total assistance (US$ Million)[14]	835.75
Of which: Fund assistance (US$ million)	19.17
(SDR equivalent in millions)	14.73
Completion point date	October 2004

Disbursement of IMF assistance (SDR million)

Assistance disbursed to the member	14.73
Interim assistance	5.62
Completion point balance	9.11
Additional disbursement of interest income[15]	1.69
Total disbursements	16.42

VIII. Safeguards Assessments:

Under the Fund's safeguards assessment policy, the Central Bank of Madagascar (BCM) is subject to a safeguards assessment with respect to the PRGF arrangement, which was approved on March 1, 2001. An off-site safeguards assessment of the BCM, which was completed on November 21, 2001, identified weaknesses and made appropriate recommendations, as reported in www.imf.org. These weaknesses are being addressed with the assistance of MFD; in particular, the BCM complete financial statements for 2003 were published for the first time in December 2004.

[14] Assistance committed under the original framework is expressed in net present value (NPV) terms at the completion point, and assistance committed under the enhanced framework is expressed in NPV terms at the decision point.

[15] Under the enhanced framework, an additional disbursement is made at the completion point corresponding to interest income earned on the amount committed at the decision point but not disbursed during the interim period.

IX. Exchange System and Exchange Rate Arrangements:

After April 1982, when the peg to the French franc was discontinued, the exchange rate was managed with reference to a basket of ten currencies. However, by end-1991, the authorities ceased the practice of adjusting the exchange rate to offset inflation differentials with key trading partners. The exchange rate regime is classified as independently floating. Since July, 2004, the Malagasy franc has been determined through a continuous interbank foreign exchange market system and on January 1, 2005, the Ariary (AR) replace the Malagasy franc as the country's official unit of account, at the rate of AR 1= FMG 5. The exchange rate in terms of the SDR at end-March 2005 was AR 2,928 = SDR 1.

Madagascar accepted the obligations under Article VIII, Sections 2(*a*), 3, and 4 on September 18, 1996 and maintains no restrictions on the making of payments and transfers for current international transactions.

X. Last Article IV Consultation:

Madagascar's consultation cycle is governed by the decision approved by the Executive Board on July 15, 2002. This decision stipulates that, subject to certain exceptions, an Article IV consultation with a member receiving financial assistance under a Fund arrangement is expected to be completed within 24 months of the conclusion of the previous Article IV consultation. The 2002 Article IV consultation staff report was discussed by the Executive Board on December 23, 2002.

XI. Technical Assistance:

Department	Dates	Purposes	Results of Missions
FAD	July-August 1994	Assess the decline in the country's tax effort and recommend measures to mobilize additional revenue.	Elimination of all ad hoc tax exemptions, beginning with the 1995 budget, recommended.
FAD	September 1995	Assess the need for reforming the value-added tax (VAT) and develop a strategy to improve tax and customs administration.	Broadening of the VAT base and the creation of a special office for the monitoring of transactions in the free export zone recommended.
FAD	September 1996	FAD advisor to assist the authorities in implementing the recommendations of FAD September 1995 mission. Assignment extended to March 1998.	The large-taxpayer unit established. Implementation of VAT reform continued.

Department	Dates	Purposes	Results of Missions
FAD	December 1997	Review existing tax incentives and prepare action plan to improve the performance of the tax and customs departments.	Program proposed to curtail exemptions and implement an exemption-monitoring scheme.
FAD	February 1998	Hold follow-up discussion on tax and tax administration reform program.	Schedule for the preparation and implementation of key measures established.
FAD	March 1998	Examine and assess budgetary expenditures, control, and management.	Comprehensive report prepared for the reform of budget planning, execution procedures, and control systems.
FAD	April 1998	Review important issues to be addressed in the area of customs administration.	Agenda for follow-up mission identified (July 1998).
FAD	June 1998	Conduct follow-up visit on expenditure control.	Action plan, based on the report of the FAD mission of March 1998, established.
FAD	May, September, and December 1998 and April, May, and June 1999	Hold follow-up discussions on tax and tax administration reform.	Assistance for the revision of the VAT law provided, and a VAT reimbursement system introduced for free export zone producers.
FAD	July 1998	Identify measures to strengthen customs administration.	Report prepared on duty assessment and collection procedures, the coordination between the preshipment inspection company and the customs department, the computerization strategy, and organizational issues.

Department	Dates	Purposes	Results of Missions
FAD	January 1999	Help implement earlier FAD recommendations on improving public expenditure management.	Aide-mémoire prepared on progress in harmonization of budget and treasury classifications, computerization of treasury offices, implementation of a cash management and financial plan, and implementation of a budget and accounting classification for the decentralized budget.
FAD	June 1999	Strengthen tax audit system of large-taxpayer unit.	Action program developed and agreed with the authorities.
FAD	February-March 2001	Examine and assess budgetary control and management.	Comprehensive report prepared for the reform of budget planning, execution procedures, and control systems.
FAD	January-February 2003	Examine and assess tax and customs administration.	Comprehensive action plan and report on establishment of an oversight committee prepared.
FAD	July-August 2003	Examine and assess tax policy and assist in tax policy design.	Comprehensive action plan and report on next steps prepared.
FAD	May-June 2004	HIPC Assessment and Action Plan (AAP).	Comprehensive action plan established.
MFD	August 1993–99	Assign a bank supervision advisor and assist in the adoption of an interbank foreign exchange market.	Supervisory agency strengthened.
MFD	April-May 1994	Review the modalities for liberalizing the exchange regime and accompanying monetary and credit measures.	Interbank exchange market adopted in May 1994. Central bank base rate and reserve requirements increased.

Department	Dates	Purposes	Results of Missions
MFD	May 1995	Review interbank foreign exchange market, develop indirect instruments of monetary management, and reduce banks' excess reserves.	Recommendations adopted during the second half of 1995.
MFD	October-November 1998	Assess the operation of the foreign exchange and treasury bill markets; introduce the euro quotation currency.	Recommendations for treasury bill market adopted in November 1998.
MFD	December 1998	Prepare the change to the euro as pivot currency.	Euro introduced as scheduled.
MFD	May-June 1999	Prepare for introduction of continuous-quotation foreign exchange market, including procedures manual and market rules.	To be implemented by end-2003.
MFD	October-November 1999	Assess exchange regulations and compliance with the Basel Core Principles for effective banking supervision.	Recommendations on banking regulation implemented in 2004d.
MFD	November-December 2002	Assess progress in the implementation of the Core Principles for effective banking supervision; and examine the early warning system for detecting bank failures.	Recommendations being implemented.
MFD	November 2002	Take an inventory of microfinance institutions and define a strategy for their supervision.	Recommendations being implemented.
MFD	November 2002	Assess management of foreign reserves and propose concrete steps for its improvement.	Recommendations being implemented.

Department	Dates	Purposes	Results of Missions
MFD	March 2003	Review central bank internal audit functions.	Awaiting final report.
MFD	March 2003	Review microfinance regulation.	Awaiting final report.
MFD	June 2003	Review currency reform.	Recommendations being implemented.
MFD	September 2004	Review operations of the newly installed interbank foreign exchange market.	The report is being finalized.
MFD	November-December 2004	Strengthening of banking supervision.	The report is being finalized.
MFD	February-March 2005	Review monetary and exchange operations, bank liquidity management, and banking supervision.	The report is being finalized.
STA	October 1995	Review money and banking statistics.	Recommendations for data improvements adopted.
STA	June 2001	Review balance of payments compilation system.	Recommendations for improvements accepted and being adopted.
STA	July-August 2001	Review money and banking statistics.	Recommendations for data improvements accepted and being adopted.
STA	February 2004	Multisector statistics mission.	Recommendations for data improvements accepted.

XII. Resident Representative:

Madagascar has had a Fund Resident Representative since September 1989. Mr. Samir Jahjah took up the post of Resident Representative at end-September 2003.

Madagascar: Relations with the World Bank

(As of April 2005)

Partnership in Madagascar's Development Strategy

45. The Government's poverty reduction strategy (PRSP) was endorsed by the World Bank and IMF Boards in November 2003. The Strategy outlines a framework for the Government to redouble its efforts to implement a new generation of economic and social reforms. The Strategy was developed over three years, starting under the previous administration and continued by the new Government. The overarching goal of the PRSP is to cut the poverty rate by half in ten years, from 70 percent in 2003 to 35 percent in 2013. To reach this objective the Strategy, based on the principle of public private partnership, has three main axes (i) restoring rule of law and a well governed society; (ii) promoting economic growth with a large social base, and (iii) promoting systems for establishing human security and enlarging social protection. Fifteen policy areas and corresponding measures, proposed outputs and expected outcomes underpin these strategic axes. The main areas are to improve governance, create a business friendly environment for investment and accelerate private sector led growth and improve social service delivery to the benefit of its citizens. The Government prepared its First Annual PRSP Progress Report in July 2004.

46. In November 2004, the Government articulated a vision up to 2015 Madagascar Naturellement. While recognizing the enormous potential of Madagascar, this vision puts a renewed focus on rural development, through the roads program, education and health and establishing better linkages between the urban and rural areas, and increasing the value added in agriculture. The vision sees a transformation of Madagascar from a subsistence economy to a market economy, increased exports, and enhanced linkages between rural economy and the industrial economy through agro-industries, pharmaceuticals, textiles and the transformation of mineral products, and through economic services such as tourism and agricultural credit. The key priorities identified include the reinforcement of the effectiveness of Government, good governance, infrastructure, education for all, rural development and environment, drinking water for all, health and AIDS prevention, private sector development, and tourism. These priorities are formulated as national programs, and there is a strong focus on integrating donor interventions into the national programs.

47. A summary of IMF-World Bank collaboration in Madagascar is provided in Table 1. The IMF leads in supporting Madagascar's medium-term program for maintaining macroeconomic stability. In March 2001, the IMF approved a Poverty Reduction and Growth Facility (PRGF) which expired on March 1, 2005. The goal of the PRGF-supported program is to support Madagascar's efforts to foster macroeconomic stability, promote accelerated growth, improve social services, and reduce poverty. It focuses on strong fiscal consolidation to lower public debt and structural reforms including: (i) monetary policy and financial sector

reform; (ii) improvement in tax administration; (iii) restructuring/privatization of public enterprises; and (iv) trade reforms.

48. The World Bank leads the policy dialogue in structural and institutional reforms aimed at: (i) strengthening governance in the public sector; (ii) accelerating pro-poor economic growth and supporting foreign investment and private sector development; and (iii) ensuring human development and security, such as in health, education, nutrition and social protection.

Bank Group Strategy and lending operations

49. The World Bank's FY04-06 Country Assistance Strategy (CAS) for Madagascar is fully aligned to the Government's program, and refocuses the existing portfolio to better align itself to the PRSP objectives and to address the key constraints to broad based growth. In FY04, the Bank approved new projects in transport, environment and governance. The CAS also reflects a gradual transition from investment to programmatic lending with annual Poverty Reduction Credits (PRSC) starting in FY05. The first Poverty Reduction Support Credit (PRSC) addressing governance, education and nutrition was approved in July 2004. A second PRSC is under preparation and is expected to be presented to the Board in early FY06, along with an Integrated Growth Poles Project addressing infrastructure and private sector development. In addition, a repeater project for HIV/AIDS and a health supplemental credit will also go to the Board at the same time. A watershed management project is under preparation for later in FY06. Recently completed analytical work such as a Public Expenditure Review and a Development Policy Review (FY05), financial management and public procurement reviews, a Rural and Environment Sector Review, a Tourism Study, a Poverty Assessment Integrated Framework provide the foundation for programmatic lending and policy dialogue.

50. As of March 27, 2005, the Bank's current portfolio consisted of 18 projects with total commitments of US$ 956.2 million. Of that, a total of US$ 562.1 million had been disbursed (or approximately 59 percent) and US$ 169.6 million had been disbursed in FY05. Of these total current commitments, around 47 percent are in infrastructure and transport about 23 percent in rural development and environment, 10 percent in the social sector, 7 percent in energy and minerals, 6 percent in governance, 5 percent in finance and private sector development, and 2 percent in multisector HIV AIDS.

IMF-World Bank Collaboration in Specific Areas

Areas where the Bank takes the lead

51. Areas in which the World Bank takes the lead are related to specific sector advice in the areas in which the Bank has active lending operations (especially in the social sectors, infrastructure, agriculture and environment) as well as through a number of analytical studies as described above. Together with the Government and other donors, the Bank is also

involved in supporting aid coordination. This has included mobilizing US$2.3 billion over a period of four years for Madagascar's reconstruction and development program financing following the 2002 crisis, and mobilizing donor support for implementing the Government's PRSP and to the Education for All initiative.

Areas in which the IMF takes the lead

8. Areas where the Fund takes the lead role relate to policy advice and reforms with respect to (i) overall macroeconomic policies and targets; (ii) tax policy and administration; (iii) budgetary accounting; (iv) treasury procedures; (v) public sector wage policy; and (vi) monetary management and exchange rate policy (including the changeover from the Malagasy franc to the new currency, the Ariary). The Bank team actively participates in discussions between the Fund and the government in all these areas, however, especially with respect to the setting of overall macroeconomic targets as well as tax policy.

Areas of Joint Responsibility

9. IMF and World Bank staff maintain a close working relationship, especially with respect to (i) monitoring the Poverty Reduction Strategy Paper; (ii) reforms set out at the decision point of the Highly Indebted Poor Countries Initiative, which culminated in Madagascar reaching completion point in October 2004; (iii) analyses and reforms in public financial management; (iv) other governance reforms, including customs; (v) support of the privatization program; and (vi) participation in the integrated framework trade initiative. Joint policy advice between the Bank and the Fund is given on (i) budgetary procedures, including expenditure execution; (ii) the functioning of internal and external budget control institutions; and (iii) monitoring and continuation of the privatization program. Table 1 includes a short description of each of the areas and specific support from the two institutions with respect to policy advice.

TABLE 1: BANK/FUND COLLABORATION

Area	***Description***	***Specialized Advice/ Reforms Supported by Fund***	***Specialized Advice/ Reforms Supported by Bank***
Completion of full PRSP	Together with multi- and bilateral donors, Bank/Fund provided continuous technical assistance toward completion of full PRSP in 2003	Macroeconomic framework: growth, revenue, expenditure, trade projections	Poverty analysis; rural poverty study; education and health sector work
HIPC completion point reforms	Regular joint Bank/Fund supervision missions; joint preparation of HIPC 'Tracking Poverty-Related Spending' assessment and action plan	Reforms linked to budgetary accounting and controls	Reforms in education, health, rural transport sector
Public financial management	Joint Bank/Fund missions analyzing fiscal management	Tax analysis and reform, strengthening control organs; expenditure management	Budget formulation, expenditure monitoring and analysis, especially in sectors important for poverty reduction; procurement, strengthening internal and external controls.
Other governance reforms	New Government has embarked on large governance reform agenda; Bank/Fund staff work closely with UNDP/EU/AfDB staffs on assisting development of implementation plans	Customs	Anti-corruption agenda, decentralization, judicial sector reform
Privatization Program	Close joint monitoring of Government's large privatization program comprising four major and several dozen smaller public enterprises	All sectors, especially monitoring of privatization receipts of large enterprises (petroleum, telecom)	All sectors.
Integrated Framework/ Trade Analytical Work	Integrated Framework paper FY04	Macro projections for IF framework paper	Sectoral analysis for IF framework paper

10. Questions may be referred to Mr. Willem van Eeghen (202-473-2399), Country Program Coordinator for Madagascar at the World Bank.

Madagascar: Statistical Issues

52. Madagascar's database remains weak, particularly by the real sector, government finances, the balance of payments, and social indicators. The authorities are aware of these deficiencies and are working, with technical assistance from the international community, including the Fund, to strengthen their statistical system. Madagascar is a participant in the General Data Dissemination System (GDDS), and its metadata have been posted on the DSBB as of May 20, 2004. STA balance of payments and monetary and financial statistics technical assistance missions visited Antananarivo in June and July 2001, respectively. Following a request by the authorities, a multisector statistics mission was fielded during February 12-25, 2004.

Real sector

53. Production of a complete set of national accounts (benchmark data) is infrequent and depends largely on the availability of source data, whose collection is irregular. The last set of accounts was produced for 1995 and 1984. For the intermediate years, only estimates of GDP at current and constant (1984) prices broadly following the *1968 SNA* are produced. These estimates are revised frequently and are considered unreliable, due to the scarcity of source data, or their inadequate use, and to methodological shortcomings. In particular, the estimates of the agricultural activities are weak because of the unavailability of suitable information about the size and the evolution of this sector. Moreover, service activities are not properly covered and little information is available on the magnitude of the informal sector. The INSTAT envisages passage to the *1993 SNA* by implementing the ERE/TES software designed for compilation of national accounts and by changing the base year from 1984 to 2001. Significantly, in January 2002, the publication of a quarterly index of industrial production by export processing zone (EPZ) enterprises was introduced, with external technical and financial assistance. There are plans to begin developing a quarterly industrial production index (covering non-EPZ enterprises), should discussions concerning United Nations Development Program (UNDP) financial assistance be completed early.

54. A revamped consumer price index (CPI), with weights based on the 1993 household survey and covering four principal cities, was introduced in July 2000. The CPI is generally reported to Fund staff on a timely basis. Data on producer prices and nationwide employment are not available. Various considerations drive the ongoing work on the wholesale price index (WPI) renewal—the key issue being the relative importance of the commercial activities in the Malagasy economy. However, the utility of such an indicator is reduced due to the limited coverage of manufacturing products.

Government finance

55. The 2004 multisector mission found that data on central government operations are only disseminated annually, and that data on public debt are not disseminated. It recommended monthly dissemination of data on central government operations, and

quarterly dissemination of data on public debt; as well as monthly reporting of data to STA for publication in *IFS*. The mission also found significant gaps in the data coverage of GFS, and recommended that it be broadened to include public agencies that are part of central government. Finally, the mission made recommendations concerning classification and recording of transactions, as well as the calculation of domestic arrears.

56. The latest government finance statistics (GFS) data reported to STA for publication in the *GFS Yearbook* are for 2002 and cover the consolidated central government. However, many classification problems remain (requiring extensive use of adjustment entries to current expenditure), and detailed information is missing in the time series since 1996 for budgetary and nonbudgetary breakdowns and for central government debt. Madagascar does not report subannual data for publication in *International Finance Statistics.*

Balance of payments

57. Since 1984, the Central Bank of Madagascar (BCM) has been in charge of compiling and disseminating balance of payments statistics, and in 1997 it implemented the fifth edition of the *Balance of Payments Manual (BPM5)*. However, the current compilation system is flawed in many respects: the external trade data are derived from customs data, which suffer from inadequate coverage and deficient recording procedures. Moreover, significant smuggling activities, particularly related to the mining sector, further reduce the reliability of recorded trade data. Because the customs processing system has experienced numerous technical disruptions since 1998, the external trade data have limited serviceability and require many manual corrections. The current implementation of the ASYCUDA (automated system for customs data, Version 2.7) was largely completed by mid-2002, with the system installed in most customs offices. There are plans to further upgrade the customs processing system to ASYCUDA ++.

58. The multisector technical assistance mission reviewed the progress made in the transition to *BPM5* and found that the authorities had implemented the surveys to direct investment enterprises, using an upgraded international transactions reporting system (ITRS), although the results have yet to be incorporated in the balance of payments. The mission noted that the compilation system is still hampered by several recurring issues: excessive processing lags due to partial automation of customs reports; inadequate coverage, for example, of transactions and debt for the private sector, NGOs, foreign embassies in Madagascar; and transaction misclassification, e.g., debt relief obtained from multilateral financial institutions is recorded in current transfers instead of in capital transfers.

59. In addition, the export processing zones (EPZ) that process goods and reexport to a third economy are not properly identified within other business services (merchanting and other trade related services).

60. The present compilation system offers wide leeway to use available data. This is exemplified by the c.i.f./f.o.b. correction indicator of 15 percent, which is entirely attributed

to freight, while ASYCUDA and port authorities can provide separate data for freight, insurance and other categories. Data for the service and income accounts rely excessively on the ITRS reports, whose accuracy is not routinely assessed against other data sources.

61. As noted by the technical assistance mission in June 2001, the INSTAT and the BCM adjust differently customs data using different techniques and publish two distinct series of trade statistics hampering the reliability of Madagascar's external transactions.

62. The compilation of external debt statistics is generally satisfactory, and the authorities are benefiting from technical assistance by the United Nations Conference on Trade and Development (UNCTAD) in installing the latest version of the Debt Management and Financial Analysis System (DMFAS). This system is not yet fully operational; some data entry remains to be completed, and certain DMFAS modules have yet to be installed by UNCTAD technicians.

Monetary statistics

63. A STA monetary and financial statistics mission visited Antananarivo in July 2001. The 2001 mission found that the BCM implemented most of the recommendations of the 1995 monetary and financial statistics mission and further recommended (i) the widening of statistical coverage to microfinance institutions; (ii) the inclusion of the Savings Bank and Postal Administration in the "Other Depository Corporations" subsector; and (iii) the improvement in the timeliness of the BCM's balance sheet.

64. Since August 2001, the BCM is reporting monetary data monetary data to STA by e-mail for publication in *International Financial Statistics (IFS)*. After a brief interruption in data reporting due to the political crisis in 2002, regular data reporting resumed in July 2002. Data for the monetary authorities and deposit money banks through December 2004 have been published in the *IFS*.

65. The 2004 multisector mission assessed the status of the 2001 mission's recommendations and made additional recommendations to improve Madagascar's monetary statistics. Assessing the status of the previous recommendations, it found that several recommendations are pending, such as (i) improvement of the staff and computer resources of the unit in charge of the monetary statistics compilation; (ii) electronic transmission of monthly call report forms by the commercial banks to the BCM; and (iii) expansion of broad money survey to include the microfinance institutions that issue liabilities meeting the national definition of broad money for Madagascar. Furthermore, the 2004 mission recommended improvements to the source data and the compilation of statistical methodology to compile Madagascar's monetary statistics in accordance with the Fund's methodology as described in the *Monetary and Financial Statistics Manuel (MFSM).*

.

MADAGASCAR: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE

AS OF MAY 4, 2005

	Date of latest observation	Date received	Frequency of Data[6]	Frequency of Reporting[6]	Frequency of publication[6]
Exchange Rates	3/31/05	4/15/05	M	M	M
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	Aug 2004	11/21/03	M	M	M
Reserve/Base Money	2/28/05	4/15/05	M	M	M
Broad Money	3/31/05	5/17/05	M	M	M
Central Bank Balance Sheet	4/30/05	5/17/05	M	M	M
Consolidated Balance Sheet of the Banking System	3/31/05	5/17/05	M	M	M
Interest Rates[2]	3/31/05	4/15/05	Q	Q	Q
Consumer Price Index	Dec 2004	2/16/05	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	2/28/05	5/03/05	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	2/28/05	5/03/05	M	M	M
Stocks of Central Government and Central Government-Guaranteed Debt[5]	Dec 2004	3/30/05	A	I	I
External Current Account Balance	2003 Q4	7/02/04	Q	Q	Q
Exports and Imports of Goods and Services	2003 Q2	10/15/03	Q	Q	Q
GDP/GNP	2003	3/22/04	A	A	A
Gross External Debt	Sept 2003	10/15/03	A	A	A

[1]Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A); Irregular (I); Not Available (NA).

Statement by Damian Ondo Mañe, Executive Director for Republic of Madagascar
June 1, 2005

On behalf of my Malagasy authorities, I would like to express their deep appreciation to Management and staff for their continued support and policy advice. This close relationship over the years, sometimes during very difficult times, has been very helpful in guiding the authorities in their policy decisions, and have contributed much to the progress made. My Malagasy authorities wish to maintain this close relationship.

Since March 2004, Directors have had 3 occasions to examine economic and financial developments in Madagascar, in the context of reviews under PRGF arrangements. In my earlier statements, in particular, that of February 16, 2005, I described developments in 2004. The more recent data do not diverge much from those of February. They indicate considerable progress, under successive PRGF arrangements, in stabilizing the economy and laying the foundation for higher growth, but they also show that the economy remains vulnerable to shocks, and that the economic adjustment programs should be pursued steadfastly and strengthened in certain areas.

My Malagasy authorities remain fully committed to the reform efforts which have received strong support from the international community, and for which they are thankful. In 2004, Madagascar reached the completion point under the HIPC Initiative and is benefiting from debt relief. The last PRGF arrangement came to a successful conclusion in March 2005, and my authorities would like to continue the close relationship with the Fund in the context of a successor PRGF that will focus on raising the growth rate. The continued vulnerability of the economy to both domestic and external shocks would justify this new program.

Recent Economic Developments

As I noted above, developments have not diverged much from the February assessment. They confirm that real GDP growth remains relatively strong at 5.3 percent, despite a number of exogenous shocks. Most sectors, in particular those of agriculture, construction, tourism, transport and textiles and garments made strong contribution to growth, which was also helped by the donor-financed capital expenditure.

Two unfavorable developments were in regard to inflation and the exchange rate. The Malagasy franc depreciated significantly in 2004 due to larger than expected demand for foreign currency by private importers in response to the tax and tariff exemptions granted in September 2003, which have since been partially removed, increased government capital expenditure and lower vanilla exports due to the cyclones. Higher world price of oil and rice contributed both to the depreciation and the higher inflation. Weakness in the foreign exchange market and at the central bank were also factors in the depreciation of the currency. A number of strong measures, under the advice of Fund staff, were put in place in the second half of 2004, both in regard to the implementation of monetary and exchange rate policy as well as in regard to structural and administrative measures. The authorities also maintained a tight fiscal policy. In particular, it should be noted that, despite the large increase in prices and strong pressures to increase wages, the government kept its commitment to the Budget. It also improved its coordination with the central bank. These have been successful in containing inflationary pressures and stabilizing the exchange rate. Recent data show that inflation peaked in February and has since fallen sharply. The authorities are fully determined to maintain strong policies so as to restore macroeconomic stability.

Monetary policy has remained tight. Net reimbursement by the Treasury to the central bank enabled an increase in credit to the private sector. The financial sector continued to strengthen in 2004, with improved profitability and prudential indicators for the banking sector. The ratio of nonperforming loans to total gross loans fell from 19.6 percent in 2002, the year of the major political crisis, to 11.4 percent in 2004. While the expansion of credit has contributed to the fall in the NPL ratio, it should be noted that there has also been major improvements in maintaining the quality of the loan portfolio. A Financial Sector Assessment Program (FSAP) is underway and the authorities look forward to its conclusion and recommendations, with a view of strengthening the sector further. The central bank has also started to implement the recommendations of the Stage One Report of the Safeguards Assessment with the help of the Monetary and Financial Systems Department of the Fund. The anti-money laundering legislation adopted in 2004 became operational this year.

In the fiscal sector, revenue performance improved in 2004, on the basis of strong reform implemented at customs, and reached 10.9 percent of GDP, compared to 10 percent in 2003. Capital outlays were higher than projected due to higher-than-expected foreign financed investment. Although the current outlays of the central government were within Budget, insufficient control over expenditure of decentralized governments bodies and public entities caused some expenditure overruns, which were compensated for by cuts in other central government outlays. Overall, the fiscal deficit, including grants, was 4.9 percent of GDP, compared to 4.2 percent in 2003, and the government reduced its domestic debt by about 2.8 percent of GDP.

In the external sector, exports of clothing, especially to the U.S., under the AGOA, increased, but export of vanilla fell significantly. Imports saw a major increase, especially of capital goods, so that the external current account deficit widened to 14 percent of GDP in 2004. The external debt position remains difficult, despite the debt relief obtained under the HIPC Initiative. At end-2004, the NPV of debt-to-exports ratio was estimated at 202.1, and will be 169.8 at end-2005. The ratio will fall below the thresholds only with additional bilateral aid beyond the HIPC Initiative. My authorities continue to make strong efforts to obtain full HIPC Initiative assistance, and have contacted all non-Paris Club creditors. They have already signed agreements with some Paris Club members, and are in discussion with others to obtain additional debt relief.

The program of structural reforms was pursued steadily in 2004, with good progress in the area of privatization, and in the improvement of the business and legal environment. Measures to improve governance have also been taken. These should contribute to lower domestic costs of doing business in Madagascar and also help to attract foreign investors.

Medium Term Policies

The objective of the authorities for the medium term is to build on the progress achieved and put in place policies, consistent with the PRSP, and that will enable Madagascar to raise its annual growth rate to a higher level, 6 percent or above, which would help the country to make progress towards the achievement of the MDGs. While structural policies and investment on infrastructure should help to improve competitiveness and create more investment opportunities for the private sector, the authorities will also pursue strong macroeconomic policies aimed at raising government revenue and keeping inflation low. The authorities expect much from foreign direct investment and donor assistance. In this regard, the authorities are pleased that Madagascar was the first country selected by the U.S. Millennium Challenge Corporation (MCC). Assistance under the MCC will focus on land reforms, financial sector development and agricultural.

Efforts to raise government revenue will be pursued, and measures will include a comprehensive reform of the tax system. The authorities will maintain a tight control over expenditure, and a number of steps are being taken to strengthen public expenditure management. Strengthening of governance at customs will remain a priority**.** Monetary policy will continue to aim at reducing inflation, while ensuring the financial needs of the developing private sector are met. To encourage the development of small enterprises, a law establishing the legal framework for microfinance operations is expected to be approved by parliament this year. The strengthening of banking supervision and improving the effectiveness of monetary policy will remain a priority for the monetary authorities.

However, in spite of the extensive reforms being made, the authorities have concerns about the medium term, in particular, as regards the textile and garments industry, which up to now have contributed significantly to growth and the creation of employment, and which will face increase competition with the expiration of the Agreement on textiles and Clothing and also with the expected termination of the AGOA by 2007. The authorities expect that the ongoing program of structural reforms will help to diversify the productive base, but this may take some time to bear results. The development of the tourism industry and agriculture, among others, are being encouraged, as well as that of other industries, including mining. The authorities expect substantial increase in regional trade through their adhesion to COMESA and SADC.

Ex Post Assessment

My Malagasy authorities agree broadly with the ex post assessment paper. Despite the fact that the political situation, over the past decade, had been unstable, important progress was made in the area of macroeconomic stabilization, although my authorities would have preferred that it had not relied so much on expenditure compression. It is true that revenue mobilization had been less successful than had been anticipated, but it should be recognized that a large segment of the population lives on less than a dollar a day, and contribute little to government revenue. Moreover, during the last few years, Madagascar has been implementing a large reduction in custom tariffs, including in the context of regional agreement. The country has also suffered from natural shocks such as cyclones, locusts infestation, etc, which have had a severe adverse impact on agricultural production and export, a main source of revenue. The government has thus experienced a loss of income, which has not been fully made up through the VAT. Nevertheless, a number of important reforms have been put in place in tax and custom administration, the issue of corruption is being addressed forcefully, and additional revenue-increasing measures are being taken. The revenue-to-GDP ratio is increasing gradually, and my authorities are confident that as economic activity increases, especially, in view of the reforms undertaken, there will be an increase in the tax ratio. It is therefore doubtful if a tougher approach, as suggested in the EPA paper, would have worked.

My Malagasy authorities agree that the structural reform agenda did take some time to produce results. In the early nineties, program ownership was weak, as reforms were more or less imposed. The difficulty to build a consensus caused progress to be uneven. However, as the paper rightly recognizes, structural reforms have been more successful in the past few years, as there have been a better and broader consultation on the reform measures, with more flexible conditionality. The linkage with the PRSP, a document that has broad popular acceptance has also helped. The authorities intend to build on the recent progress to accelerate the reform process, and create the conditions for the development of a strong private sector which will be the engine of growth.

However, and more importantly, the difficulty encountered showed that lack of capacity played an important role in the failure to implement many policy measures. The inability of the civil service to attract sufficient numbers of skilled staff, due to low very low salaries, have hindered progress in many sectors, including the judicial system. Madagascar has made use of technical assistance from the Fund and other multilateral institutions and donors, but this has not been enough, and often the newly trained personnel left the service. My authorities are giving full attention to the issue of capacity-building. In this regard, they are finalizing a time-bound technical assistance plan which will prioritize their needs. The plan will then be presented to donors and a coordinated deliver process will be put in place.

Finally, as noted in the EPA paper, Madagascar is making good progress in its reform process, but the economy remains weak and vulnerable. It will continue to require balance-of-payments assistance over the medium term. Without external assistance, it is unlikely that the MDGs will be achieved. For their part, my Malagasy authorities are fully committed to continue the adjustment process. They are of the view that Madagascar is at a crossroad, and that it will be important to build on the progress achieved. They therefore would like to request continued Fund support in the form of a successor-PRGF arrangement. They also hope that donors will continue to give the country their full support, and that Madagascar will benefit from further debt relief assistance.

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 05/131
FOR IMMEDIATE RELEASE
September 27, 2005

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2005 Article IV Consultation with the Republic of Madagascar

On June 1, 2005, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with the Republic of Madagascar.[1]

Background

Since the mid-1990s, Madagascar has made significant progress in terms of macroeconomic stabilization and structural reform. Political stability has been broadly restored following the disputed 2001 presidential elections and the ensuing political crisis. Since that time, the authorities have taken measures to reestablish investor confidence and private sector growth was reinvigorated. Key structural reforms were implemented, albeit with significant delays, in particular in the area of public enterprise reform and the fight against corruption. However, the economy remains vulnerable to shocks, including cyclones, and policy slippages. Progress in domestic revenue mobilization and in strengthening the budget process also remained modest, reflecting in part the country's limited institutional capacity. Madagascar reached the completion point under the enhanced Heavily Indebted Poor Countries (HIPC) Initiative in October 2004.

Macroeconomic developments in 2003 and 2004 were dominated by the sharp depreciation of the national currency, and rising inflationary pressures, with year-on-year consumer price inflation reaching 30 percent at end-February 2005. At the same time, the current account deficit widened considerably in 2004, reflecting the significant decline in the volume of vanilla exports and the surge in imports following, among other factors, the tax and tariff exemptions

[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.

granted in 2003. In spite of a disappointing revenue performance and some expenditure overruns toward the end of the year, the public finances position strengthened in 2004, as the authorities were able to contain overall expenditures, and particularly wages, in the difficult context of mounting inflationary pressures.

In the medium term, real GDP growth is expected to average 6 percent per annum and fiscal consolidation is projected to continue, driven by an improvement of the revenue performance and modest expenditure increases. The current account position should also improve over the medium term. While remaining fragile, the external debt position should remain sustainable, provided the authorities continue to limit new external financing to grants and to highly concessional loans. There are several risks to this outlook however, especially in the external sector, where the impact of the expiry of preferential agreements on textiles exports could turn out to be larger than currently expected.

Executive Board Assessment

Executive Directors commended the Malagasy authorities' greater ownership of economic policies and consequent improved track record of policy implementation in recent years. They welcomed Madagascar's improved growth performance, the authorities' success in stabilizing the exchange rate in the second half of 2004, and the strengthening of the external reserve and debt positions. However, Directors noted that poverty remains prevalent and the external debt vulnerable, and that major uncertainties surround Madagascar's medium-term outlook. They therefore welcomed the authorities' commitment to contain inflation, preserve Madagascar's competitiveness, and gradually build-up official reserves. This commitment, together with accelerated progress on structural reforms and the assistance of the donor community, will be crucial for Madagascar to attain macroeconomic stabilization and the Millennium Development Goals.

Directors stressed that containing inflation, a key macroeconomic objective for 2005, hinges on the steadfast and timely implementation of the envisaged tight monetary and fiscal policies as well as on the evolution of the world prices of oil and rice. Directors welcomed the recent measures taken to improve coordination within the Ministry of Finance and between the Ministry of Finance and the central bank.

Directors expressed disappointment that Madagascar's revenue performance remains weak—reflected in a relatively low revenue-to-GDP ratio—despite prolonged Fund engagement with the country, substantial technical assistance, and the significant customs reforms implemented. They attached high priority to a coherent and predictable tax policy that eschews ad hoc tax exemptions, and to continued strengthening of tax and customs administration. They welcomed the authorities' commitment to pursue medium-term, revenue-enhancing policies in the context of a comprehensive reform of the tax system, and urged the authorities to forge a consensus on the tax reform's goals and strategy.

Directors welcomed the measures taken to avoid the recurrence of the spending slippages that took place in 2003 and 2004, including better control of military wages and the elimination of emergency spending procedures. They emphasized that further strengthening of public expenditure management, including better alignment of the budget with the priorities of the

PRSP and proper monitoring of how resources freed by the HIPC Initiative are spent, will be critical for improving the quality and efficiency of public spending. They also encouraged implementation of a comprehensive civil service reform.

Directors encouraged the central bank to take further steps to improve the effectiveness of monetary policy, and to be more proactive in managing liquidity. In this regard, they welcomed the authorities' intention to implement the recommendations of a recent Fund technical assistance mission. They also endorsed the authorities' flexible exchange rate policy, which limits exchange market intervention to smoothing operations, and agreed that the current exchange rate appears to be broadly appropriate. Directors commended the recent efforts to improve the financial system and the progress made in implementing the recommendations of the safeguards assessment report. They encouraged the authorities to strengthen banking supervision further, and looked forward to the findings and recommendations of the ongoing Financial Sector Assessment Program.

Directors stressed that structural reforms are necessary to diversify the export base and maintain external competitiveness in the period ahead. The expiration of the Agreement on Textiles and Clothing in 2005 and the expected end of the third-party apparel provision of the United States' African Growth and Opportunity Act in 2007 reinforce the importance of strengthening competitiveness. Directors were therefore encouraged by the recent pick-up in the pace of structural reform, and urged the authorities to maintain the momentum. They welcomed the lowering of external trade barriers, and emphasized the need for complementary measures to promote a competitive business environment, including the development of a comprehensive strategy for the utilities sector. Land ownership rights and registration remain critical issues that should be resolved as soon as possible. Directors welcomed the creation of the anti-corruption bureau, and more generally the government's efforts to become more transparent, and urged the authorities to continue to implement vigorously the anti-corruption reform program.

Directors welcomed Madagascar's attainment of the completion point under the enhanced HIPC Initiative in October 2004. They supported the authorities' efforts to obtain full HIPC assistance from all creditors, and recommended a prudent borrowing policy and strengthened debt management to preserve external debt sustainability.

Directors observed that Madagascar's limited absorptive and institutional capacity has adversely affected the implementation of structural reforms, and urged the authorities to address this issue promptly with the help of the international community, including the IMF. They underscored that shortcomings in economic and social data hamper policy formulation, implementation, and monitoring. Directors stressed the need to finalize the action plan for capacity building, especially at the Ministry of Finance, the central bank, and the statistical institute, in 2005. Directors emphasized that coordinated and steady donor support will be crucial for the success of the authorities' capacity-building efforts.

Directors generally agreed with the main findings and recommendations of the ex-post assessment report. In particular, they concurred that a successor PRGF arrangement could help Madagascar achieve its poverty reduction goals and make significant progress toward the attainment of the Millennium Development Goals, at a time when the economy remains vulnerable and foreign reserves fairly low. Among the lessons to be learnt for future program design, Directors highlighted the importance of structuring conditionality so as to reinforce the fiscal revenue base, improve public expenditure management, accelerate capacity building efforts, and implement policies that maintain Madagascar's competitiveness. It will also be important to continue to build national ownership of policies through a close dialogue with civil society. Furthermore, better alignment of technical assistance with policy priorities will be crucial to improve the effectiveness of such assistance.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case. The staff report for the Article IV consultation with the Republic of Madagascar may be made available at a later stage if the authorities consent.

Madagascar: Selected Economic Indicators

	2001	2002	2003	2004 Est.
	(Annual percent change, unless otherwise indicated)			
National accounts and prices				
Change in real GDP	6.0	-12.7	9.8	5.3
Change in consumer prices (end of period)	4.8	13.9	-0.8	27.0
Money and credit				
Broad money (M3)	-4.8	39.9	8.2	23.0
External sector (in terms of SDRs)				
Exports, f.o.b.	20.6	-50.5	79.4	-3.9
Imports, c.i.f.	5.5	-37.6	73.7	17.7
Current account balance (in percent of GDP)				
including official transfers	-1.3	-6.0	-4.9	-10.6
excluding official transfers	-2.0	-6.1	-7.5	-14.4
Gross official reserves (in millions of SDRs)	317.5	266.6	284.4	333.5
(in months of imports of goods and nonfactor services)	3.3	4.1	2.7	2.8
	(In percent of GDP)			
Public finance				
Overall government balance				
Including grants	-4.3	-5.5	-4.2	-4.9
Excluding grants	-8.2	-7.7	-9.3	-13.1
Tax revenue	9.7	7.7	10.0	10.9
Poverty				
National poverty rate (in percent of total population)	69.0			

Source: Malagasy authorities.