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July 11, 1983

To: Members of the Executive Board

From: The Acting Secretary

Subject: Dominica - Staff Report for the 1983 Article IV Consultation, Review Under Extended Arrangement, and Program for 1983/84

Attached for consideration by the Executive Directors is the staff report for the 1983 Article IV consultation with Dominica, a review under the extended arrangement, and the program for 1983/84. A draft decision appears on pages 21 and 22.

This subject will be brought to the agenda for discussion in the first week of August prior to the Board recess.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. Ewart S. Williams, ext. 77189.

Att: (1)

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INTERNATIONAL MONETARY FUND

DOMINICA

Staff Report for the 1983 Article IV Consultation, Review Under Extended Arrangement, and Program for 1983/84

Prepared by the Staff Representatives for the 1983 Article IV Consultation with Dominica

Approved by J. Ferran and W. A. Beveridge

July 8, 1983

I. Introduction

The 1983 Article IV consultation discussions with Dominica were held in Roseau in the period May 20-June 3, 1983.1/ At the same time, the staff conducted a review of developments under the extended Fund facility program and discussed performance criteria to cover the final seven-month period of the arrangement beginning July 1, 1983. The Dominica representatives at these discussions included the Prime Minister, who is also Minister of Finance, other Ministers of the Cabinet, the Financial Secretary, and other government officials. The staff representatives were Messrs. Williams (Head), Habanananda, Khor, and Zeas (all WHD), and Mrs. Dass (Secretary-TRE). The mission was accompanied by Mr. Gerard Byam, a member of the Inter-Agency Resident Mission, who assisted in the review of the public investment program. Mr. Michael Casey, Alternate Executive Director, participated in the principal policy discussions.

In February 1981, the Executive Board approved a three-year extended arrangement with Dominica for SDR 8.55 million, the equivalent of 295 per cent of quota (EBS/81/12 and EBM/81/18). At the same time approval was given for a purchase under the compensatory financing facility, raising Fund holdings under that facility to 100 per cent of quota. Dominica has made all available purchases (SDR 7.12 million) under the extended Fund facility arrangement to date. As of May 31, 1982, Fund holdings of Dominica currency totaled SDR 13.5 million (447 per cent of quota), including SDR 2.8 million (96 per cent of quota) under the compensatory financing facility. Full use of the extended arrangement would raise the Fund's holdings of Dominica's currency to 496 per cent of quota, including 76 per cent of quota under the compensatory financing facility (Table 1). Further information on Dominica's relations with the Fund is presented in Appendix A.

In the attached letter to the Managing Director, dated June 3, 1983, the Prime Minister and Minister of Finance of Dominica reviews developments under the extended arrangement and describes the policies

1/ Dominica has accepted the obligations of Article VIII, Sections 2, 3, and 4.

Table 1. Dominica: Projection of IMF Position over EFF Program

	Jan.	Jan.		Feb.	May	Aug.	Nov.	Feb.
	1981	1982	1983	1983	1983	1983	1983	1984
	(In millions of SDRs)							
Purchase (cumulative)	1.65	6.48	9.33	10.04	10.75	11.23	11.72	12.18
Credit tranches - stand-by	0.70	0.73	0.73	0.73	0.73	0.73	0.73	0.73
Compensatory financing	0.95	2.90	2.90	2.90	2.90	2.90	2.90	2.90
Extended Fund facility	--	1.43	2.85	3.21	3.56	3.80	4.04	4.28
Supplementary financing under extended Fund facility	--	1.43	2.85	3.21	3.56	3.80	4.05	4.28
Schedule repurchase	--	--	--	--	0.12	0.24	0.47	0.71
Net purchases	1.65	6.48	9.33	10.04	10.63	10.99	11.25	11.47
Total holding (end of period)	4.55	9.38	12.22	12.94	13.53	13.89	14.15	14.37
Excluding compensatory and oil facility	3.60	6.48	3.33	10.04	10.75	11.23	11.72	12.18
	(In per cent of quota)							
Total holdings	156.90	323.45	421.48	446.05	466.52	478.97	487.93	495.52
Excluding compensatory and oil facility	124.14	223.45	321.48	346.05	370.69	387.24	404.14	420.00

Source: Fund staff estimates.

of the Government and its financial program for 1983/84. Up to SDR 1.41 million will be available to Dominica in the period July 1983-February 1984.

II. Background

Dominica is one of the smallest and least developed islands in the Eastern Caribbean with a population of less than 80,000 and per capita GDP equivalent to about SDR 800 in 1982. Bananas provide the main livelihood for some 6,000 farmers (out of a labor force of about 30,000) and constitute some 50 to 60 per cent of exports. Manufacturing contributes less than 10 per cent of GDP but has made a substantial contribution to foreign exchange earnings in the last two years. The economy is heavily dependent on private remittances and foreign aid.

In 1979 and 1980, hurricanes devastated the agricultural sector and caused severe damage to roads, port installations, and electricity generation and transmission facilities. This, combined with political and social instability, led to a 17 per cent decline in real GDP in 1979. In 1980 an upsurge in construction activity related to rehabilitation works and a sizable expansion of manufacturing output brought real GDP back to its 1978 level, but the weakness in the public finances and the balance of payments caused by the hurricane damage persisted.

The extended arrangement approved in February 1981 was to provide the framework for an economic recovery effort. The arrangement was primarily designed to (a) effect a structural improvement in public finances by raising public sector savings; (b) promote higher levels of foreign aid and investment; and (c) reorient the investment effort in a manner that would strengthen the balance of payments position in the medium term. The fiscal plan, the main policy instrument, called for raising the level of government revenues and maintaining tight restraint on the growth of current expenditure. The latter was to be achieved through a moderation of wage increases, a hiring freeze throughout the Central Government, and the elimination of budgetary transfers to the rest of the public sector. With the aid of these measures, the Central Government's current deficit was to be reduced from over 18 per cent of GDP in 1979/80 to less than 11 per cent of GDP in 1980/81, and to 2.8 per cent of GDP in 1981/82, the first full fiscal year covered by the extended arrangement; a near balance of central government current operations was programed for 1982/83 to be followed by a small surplus in 1983/84.

With the assistance of the IBRD, the authorities formulated a three-year investment program which focused on the restoration and improvement of infrastructure, the diversification of agricultural production, and the promotion of industrial development. The program envisaged increasing the level of public sector investment from the equivalent of 12 per cent of GDP in 1979/80 to 21 per cent of GDP in 1982/83. Because of this sharp increase in investment, the overall deficit of the Central Government was programed to decline only slightly from 24 per cent of GDP in 1980/81 to 21 per cent of GDP in 1982/83. These deficits were to be largely financed by concessionary grants and loans and nonconcessionary financing was programed to be reduced from 8 per cent of GDP in 1980/81 to 4 per cent in 1982/83. The program specifically provided for a phased reduction in the public sector's dependence on banking system credit so as to leave more credit available for the private sector. The demand management strategy was intended to be consistent with a reduction in the balance of payments deficit on current account from the exceptionally high level of 1980 (56 per cent of GDP) to about 26 per cent of GDP in 1983.

III. Recent Developments and Performance Under the EFF

Dominica's performance under the extended arrangement so far has been satisfactory. The adjustment in the public finances has been significant despite sluggish government revenues in 1982/83 and the constraints imposed by the three-year wage agreement which runs through 1984. Many of the essential rehabilitation works included in the public investment program have been completed and much progress has been made on the agricultural diversification program. One high priority project--the road rehabilitation program--has proceeded more slowly than anticipated because of problems of project preparation and implementation and administrative delays in finalizing arrangements with donor countries. With regard to the balance of payments, the current deficit was cut by nearly two thirds from 1980 to 1982, a reduction which was larger than envisaged in the program. Dominica made all but one of its purchases on schedule. Failure to meet performance criteria in June 1982 led to a temporary suspension of drawing rights until the following quarter when the performance criteria were met.

Real GDP rose by 8 per cent in 1981 based on a strong recovery in banana production (which rose from 13,500 tons to 34,200 tons) and continued growth in other agricultural production and manufacturing; output of the construction sector, which in 1980 had been boosted by the large-scale reconstruction and rehabilitation activity, declined sharply in 1981.

The growth in real GDP slowed to just over 3 per cent in 1982. Value added in agriculture grew by 5 per cent, reflecting a smaller growth in banana production, and value added in the manufacturing sector rose by 10 per cent, somewhat less than in 1981. Value added in the distributive trades did not increase in 1982 and construction activity declined for the second consecutive year. The annual rate of inflation, which rose to 30 per cent in 1980 under the impact of food shortages, fell to 14 per cent in 1981 and, with the sharp deceleration in import prices, to only 4 per cent in 1982 (Table 2).

Table 2. Dominica: Principal Economic Indicators

	1978	1979	1980	1981	1982	Projection 1983	Projection 1984
(In millions of East Caribbean dollars)							
Nominal GDP at market price	120.6	112.8	156.3	181.7	194.4	213.6	240.3
Fiscal year GDP (ending June 30)	108.9	116.7	134.6	169.0	188.1	204.0	227.0
(Percentage change)							
Nominal GDP at market price	24.0	-6.5	38.6	16.3	7.0	9.9	12.5
Real GDP	12.0	-17.2	17.0	8.0	3.3	5.3	7.2
GDP deflator	11.4	20.6	16.1	0.1	2.7	4.0	4.0
Consumer price index	7.7	19.9	29.8	13.9	4.4	6.0	6.0

Source: Ministry of Finance, Trade, and Industry.

With the strong recovery in banana exports and a doubling in exports of soap, the current account deficit of the balance of payments was reduced from US$33 million (56 per cent of GDP) in 1980 to US$21 million (32 per cent of GDP) in 1981; continued strong export growth combined with a fall in the level of imports led to a further reduction in the current account deficit to US$13 million, or 19 per cent of GDP in 1982 (Table 3). The EFF program had projected a current account deficit for 1982 equivalent to 29 per cent of GDP.

In line with program targets, the deficit on central government current operations declined from EC$25 million (18 per cent of GDP) in 1979/80 to EC$5 million (2.9 per cent of GDP) in 1981/82. Domestic revenue rose by 80 per cent over these two fiscal years, from the equivalent of 23 per cent of GDP in 1979/80 to 31 per cent of GDP in 1981/82. In the same period, current expenditure fell from 41 per cent of GDP to 33 per cent of GDP; the wage bill rose by close to one half, reflecting the annual 10 per cent adjustment in basic wages and the payment of backpay for 1979/80, but transfers to the rest of the public sector fell markedly. With the improvement in current operations the overall deficit (before grants and concessionary loans) narrowed from almost 30 per cent of GDP in 1979/80 to 15-1/2 per cent in 1981/82. Budget support grants from abroad, which had reached exceptional levels (25 per cent of GDP) in the aftermath of the hurricane, declined to 8 per cent of GDP, with nonconcessionary financing remaining at about 6 per cent of GDP (Tables 4 and 5).

In 1982/83, the current operations of the Central Government are estimated to have registered a deficit of EC$3.5 million (1.7 per cent of GDP) instead of the virtual equilibrium projected in the program.

Table 3. Dominica: Projected and Actual Balance of Payments

	1980 Actual	1981 Orig. EFF Proj.	1981 Actual	1982 Rev. EFF Proj.	1982 Est.	Proj. 1983	Proj. 1984
	(In millions of U.S. dollars)						
Current account balance	-32.5	-18.4	-21.6	-20.8	-13.3	-14.0	-14.2
Trade balance	-43.5	-28.0	-30.6	-28.2	-23.0	-23.9	-24.6
Exports, f.o.b.	(9.7)	(20.5)	(19.1)	(19.0)	(24.5)	(26.3)	(31.0)
Imports, c.i.f.	(-53.2)	(-48.5)	(-49.7)	(-48.3)	(-47.5)	(-50.2)	(-55.6)
Travel (net)	1.7	4.8	2.2	2.2	3.0	3.9	4.1
Other services (net)	0.3	-1.2	0.6	0.3	-0.3	-1.3	-1.7
Insurance receipts	2.7	0.4	0.4	--	--	--	--
Private transfers	6.3	5.6	5.8	6.0	7.0	7.3	8.0
Capital (including official grants)	32.7	12.2	16.1	17.5	10.3	11.8	15.6
Official transfers (net)	17.8	7.8	9.1	9.1	6.0	8.0	10.7
Official loans	1.4	3.0	5.0	7.2	7.1	5.8	4.9
Financial intermediaries	7.3	1.1	4.0	1.2	-3.7	-2.0	--
Other and errors and omissions	6.2	--	-2.0	--	0.9	--	--
SDR allocation	0.3	0.3	0.3	--	--	--	--
Overall balance	0.5	-6.2	-5.2	-3.3	-3.0	-2.2	1.4
Financing	-0.5	6.2	5.2	3.3	3.0	2.2	-1.4
Net ECCA position	--	0.1	0.7	--	--	--	--
Net IMF position	-0.3	5.5	4.6	3.3	3.3	2.3	-1.4
Net foreign assets	-0.2	0.6	-0.1	--	-0.3	-0.1	--
	(In per cent of GDP)						
Trade balance	-75.1	-39.5	-45.5	-39.0	-31.9	-30.2	-27.6
Current account balance	-56.1	-26.0	-32.1	-28.8	-18.5	-17.7	-16.0
Overall balance	0.9	-8.8	-7.7	-4.6	-4.2	-2.4	1.6

Sources: Ministry of Finance, Trade, and Industry; and Fund staff estimates.

Table 4. Dominica: Central Government Operations

	1978/79	1979/80	1980/81	1981/82	1982/83 Prog.	1982/83 Est.	Prog. 1983/84
	(In millions of East Caribbean dollars)						
Domestic revenue	25.7	31.5	48.0	56.7	60.6	57.8	67.0
Tax revenue	23.6	27.4	42.8	50.1	54.1	50.4	58.5
Other revenue	2.1	4.1	5.2	6.6	6.5	7.4	8.5
Current expenditure	32.8	56.1	65.1	62.1	61.3	61.3	67.2
Wages and salaries	16.3	25.9	36.3	38.2	36.1	35.7	38.7
Of which: backpay	(--)	(--)	(5.9)	(5.9)	(--)		
Goods and services	9.0	10.6	10.1	11.7	12.4	11.2	12.6
Interest	2.2	2.2	4.4	3.7	3.5	4.8	6.8
Pensions	1.7	1.6	2.8	3.3	2.5	4.3	3.2
Transfers	3.6	13.3	11.5	5.2	6.8	5.3	5.9
Rest of general government	(1.0)	(3.7)	(1.6)	(1.2)	(0.7)	(1.1)	(1.1)
State enterprises	(0.4)	(7.2)	(6.3)	(--)	(--)	(--)	(--)
Other	(2.2)	(2.4)	(3.6)	(4.0)	(6.1)	(4.2)	(4.8)
Hurricane relief	--	2.5	--	--	--	--	--
Current account deficit	-7.1	-24.6	-17.1	-5.4	-0.7	-3.5	-0.2
Capital expenditure	10.9	15.5	22.5	23.0	42.6	27.5	43.3
Overall deficit	18.0	-40.1	-39.6	-28.4	-43.3	-31.0	-43.5
Financing	18.0	40.1	39.6	28.4	43.3	31.0	43.5
Foreign grants and concessionary loans (net)	18.6	34.3	29.3	15.9	34.8	28.7	37.8
Budgetary grants	8.8	19.3	12.3	2.2	1.0	1.0	3.5
Project-related grants	8.1	14.9	14.7	9.9	19.7	12.7	23.6
Concessionary loans (net)	0.1	0.1	2.3	3.8	14.1	15.0	10.7
Other financing (net)	-0.6	5.8	10.3	12.5	8.5	2.3	5.7
Foreign (net)1/	-1.4	7.8	9.5	8.5	8.5	7.8	0.7
Domestic (net)	0.8	-2.0	0.8	4.0	--	-5.5	5.0
Of which: commercial banks	(1.3)	(1.1)	(-0.7)	(4.2)	(--)	(--)	(--)
	(As per cent of GDP)						
Current revenue	21.6	23.3	29.5	30.5	29.3	28.3	29.5
Current expenditure	27.5	41.5	39.9	33.4	29.7	30.0	29.6
Current account deficit	-5.9	-18.2	-10.5	-2.9	-0.3	-1.7	-0.1
Capital expenditure	9.1	11.5	13.8	12.4	20.6	13.5	19.1
Overall deficit	-15.1	-29.7	-24.3	-15.3	-20.9	-15.2	-19.2
Financing							
Foreign grants and concessionary loans (net)	15.6	25.4	18.0	8.4	16.8	14.1	16.7
Other financing (net)	-0.5	4.3	6.3	6.9	4.1	1.1	2.5

Source: Ministry of Finance, Trade and Industry.

1/ Includes IMF, ECCA, and use of foreign assets.

Table 5. Dominica: Comparison of EFF Projections and Outturn

	1979/80	1980/81		1981/82		1982/83		1983/84
	Actual	Program	Actual	Program	Actual	Program	Actual	Program
	(In millions of East Caribbean dollars)							
Central government finances								
Financing requirement	-5.8	-13.4	-10.3	-10.0	-12.5	-8.5	-2.3	-5.7 1/
	(Per cent of GDP - fiscal year basis)							
Current deficit (before foreign grants)	-18.2	-10.9	-10.5	-3.1	-2.9	-0.3	-1.7	--
Overall deficit (before foreign aid and concessionary loans)	-27.7	-23.3	-24.3	-20.9	-15.3	-20.9	-15.0	-19.2
Overall deficit (= financing requirement)	-4.3	-7.8	-6.3	-4.9	-6.8	-4.1	-1.1	-0.3 2/
	1980	1981		1982		1983		1984
				Revised				
	Actual	Prog.	Est.	Prog.	Est.	Prog.	Est.	Proj.
	(Per cent of GDP - calendar year basis)							
Balance of payments								
Current deficit (goods, services, and private transfers)	-56.1	-26.0	-32.1	-28.8	-18.5	-25.8	-17.7	-16.0

Sources: Ministry of Finance, Trade, and Industry; and Fund staff estimates.

1/ Includes EC$5 million of foreign concessionary loans and grants which were received in 1982, but now held on deposit in commercial banks.

2/ Excludes drawdowns of the earmarked deposits referred to in footnote 1.

Capital outlays, although rising by 20 per cent over the previous year, were approximately 35 per cent below program levels and the overall deficit, before grants, remained at 15 per cent of GDP.

Current expenditures in 1982/83 were held to the levels envisaged in the program, but revenues fell below projected levels mainly because of shortfalls in import and consumption duties related to the low level of taxable imports. There were expenditure overruns on interest payments (due to an underestimation in the program) and on retirement benefits related to the closure of the National Housing Corporation (NHC). To keep current spending to programed limits, the Government postponed plans for the expansion of the security forces, reduced transfers abroad and cut back on expenditures on other goods and services. The latter was facilitated by the introduction of improved accounting and budgetary procedures and the establishment of an expenditure monitoring unit within the Ministry of Finance.

The finances of the rest of the public sector have been strengthened in the last two years as the combined current deficit declined from EC$11.9 million (6.4 per cent of GDP) in 1981/82 to EC$2.5 million (1.3 per cent of GDP) in 1982/83. As a result, central government transfers to the rest of the public sector have been reduced. Transfers to the Dominica Banana Growers' Association (DBGA), which were introduced in 1979/80 following the sharp fall in export revenues, were replaced in 1981 by foreign grants and by borrowing from the domestic banking system. In 1982 despite an increase in export revenues, the DBGA reduced prices paid to farmers, reduced subsidies on fertilizers and other inputs and secured a consolidation and rescheduling of local commercial bank debts. The substantial upward adjustments made in the tariffs of the Port and Water Authorities in 1981 reduced their need for budgetary support in 1981. Rising labor costs created new strains in the finances of these enterprises in 1982, and their financial position remains quite weak.

The shortfall in capital outlays in 1982/83 was due to delays in completing preliminary work for the multi-donor road program which resulted in only about one half of the funds earmarked for roads and bridge construction being spent. In agriculture, the tree crop diversification program, which is intended to transfer marginal banana farms to the production of mangoes, avocados, citrus, and coffee continued to be implemented ahead of schedule, and significant progress was made on the coconut rehabilitation scheme and the food crop development project. In the past, the construction of factory shells, which was an integral part of the industrial development program, proceeded slowly because of the policy of the Caribbean Development Bank (CDB) which specified that demand for factory space had to be identified before funds were committed for that purpose. During 1982/83, the policy was modified and the CDB approved funding for 46,000 square feet of factory space. Additionally, approval was given for about one half of the EC$4 million of balance of payments support from OPEC to be earmarked for the construction of factory shells.

Monetary developments in 1980-81 were characterized by a slow growth in private savings and a sharp increase in credit to the private sector, which led to a reduction in the net foreign assets of the commercial banks. Commercial banks' liquidity eased markedly in 1982 as liabilities to the private sector increased by 17 per cent and the public sector reduced its indebtedness to the banking system. Private sector credit demand declined in 1982 because of the tightening of the terms of installment credit for the purchase of cars and other consumer durables and the depressed state of the distribution sector. In these circumstances the banks repaid foreign liabilities and accumulated deposits with ECCA.

IV. Report on Discussions and the 1983/84 Program

Real GDP is projected to increase by about 6 per cent a year in 1983 and 1984. The projection is predicated on an increase in banana production of about 12 per cent a year and an even stronger expansion in the output of other crops covered by the various diversification programs. Value added in manufacturing is projected to increase by an average of 8 per cent over the two years, as a leveling off in the expansion of the soap industry due to trade problems in the CARICOM area is expected to be offset by increasing output of new manufacturing plants which were established in late 1982 and in 1983; value added in construction is projected to increase sharply, reflecting the intensification of activity on the road rehabilitation program and the start of construction work on two housing schemes financed by concessionary assistance from Venezuela and Trinidad and Tobago. With the continued moderation in import prices and in the absence of any major increases in indirect taxes, the rate of domestic inflation is projected to remain in the 5-6 per cent range.

The current account deficit of the balance of payments is projected to decline to the equivalent of 18 per cent of GDP in 1983 and 16 per cent of GDP in 1984 (see Table 3). These projections assume a reduction in soap exports to CARICOM as a result of a resumption in production in Jamaica, offset by exports of the new industries (such as garments) and by higher banana exports which are projected to increase by 9 per cent in 1983 and 14 per cent in 1984 (mainly reflecting an increase in volume). All in all, total exports are projected to increase by 11 per cent in 1983 and by 19 per cent in 1984. Imports are projected to increase by about 6 per cent in 1983 and 11 per cent in 1984 largely because of higher imports of capital goods and construction materials related to the work on public investment projects: imports of consumer durables should decline, assuming a continuation of restrictions on consumer credit, and imports of edible oils should be gradually eliminated as coconut production reaches pre-hurricane levels.

Prospects for Dominica's economy over the medium term are improving. Banana production is projected to surpass pre-hurricane levels by 1985 by which time the process of agricultural diversification also should be well advanced. The expected growth of agricultural production combined with the ongoing expansion of the enclave manufacturing sector should strengthen Dominica's export base and make it more resilient to temporary fluctuations in external demand conditions. However, the achievement of a viable balance of payments will also require further adjustment measures and continuing external support. The current account deficit is not projected to reach 10 per cent of GDP until 1986. In the letter of intent, the Dominica authorities have indicated that they intend to request additional use of Fund resources following the completion of the current extended arrangement and expressed the hope that the Fund would give favorable consideration to the request.

Except for borrowings from the Fund and ECCA, most of Dominica's foreign debts are on concessionary terms with average interest rates of about 4 per cent and maturities of 15 years or more. Dominica has no foreign commercial bank loans outstanding. External debt service payments are projected to increase from US$1.4 million (5 per cent of exports of goods and services) in 1982 to US$3.5 million (12 per cent of exports of goods and services) in 1983. About one half of the increase is due to charges and repurchases to the Fund. On the basis of foreign loans outstanding as of June 30, 1983, debt service is projected to remain at about 12 per cent of GDP for at least up to 1987 because of obligations to the Fund and the servicing of CDB loans for port rehabilitation and industrial development (Table 6).

1. Fiscal policy

The Central Government's fiscal plan for 1983/84 aims at achieving approximate balance on current operations (the original program target was a small surplus) and limiting capital expenditure to levels that could be financed by available concessionary assistance. On the basis of present projections, this implies a level of capital outlays of EC$43 million, approximately 55 per cent higher than in 1982/83, and an overall deficit (before concessionary loans and grants) of 19 per cent of GDP compared with 15 per cent of GDP in 1982/83. Project-related loans and grants are projected at EC$34 million. This figure excludes EC$5 million of grants and loans which are presently held on deposit in commercial banks pending disbursement on specific projects. In addition, Dominica expects to receive between EC$4-8 million of budgetary aid from U.S. AID to be used as counterpart funds for the central government investment program. An amount of EC$3.5 million is incorporated in the fiscal program (see Table 4).

The current account target for the central government budget is predicated on the introduction of a tax package yielding EC$2.9 million (1.3 per cent of GDP) which would raise total revenue to the equivalent of 30 per cent of GDP. The revenue package, which is to be announced in the 1983/84 budget, comprises (a) an increase in the tax on sales of foreign exchange from 1 to 1-1/2 per cent; (b) an increase in consumption duties on gasoline, kerosene, and diesel; (c) the imposition of consumption duties on items imported by the External Trade Bureau (ETB); (d) the introduction of a hospital levy to be collected by the social

Exactly as agreed. July 11

Table 6. Dominica: Summary of External Public Debt Operations 1/

	1980	1981	1982	Projection 1983	1984	1985	1986	1987
	(In thousands of U.S. dollars)							
Outstanding debt at end of period	17,436	23,752	32,942	39,706	43,464	45,807	43,635	41,350
Outstanding debt at beginning of period	14,829	17,436	23,752	32,942	39,706	43,464	45,807	43,635
Net drawings	1,695	8,043	10,386	6,764	3,758	2,343	-2,172	-2,285
Drawings	(1,937)	(8,637)	(11,014)	(8,630)	(6,807)	(5,064)	(700)	(550)
Amortization (-)	(-242)	(-594)	(-628)	(-1,866)	(-3,049)	(-2,721)	(-2,872)	(-2,835)
Valuation adjustment	912	-1,727	-1,196	--	--	--	--	--
Outstanding debt at end of period (excluding IMF)	15,013	16,197	22,679	27,626	32,779	36,707	36,285	35,817
Debt service payments	649	1,073	1,401	3,524	4,875	4,742	4,812	4,461
Amortization	242	594	628	1,866	3,049	2,721	2,872	2,835
Interest	315	218	179	997	1,048	1,181	1,240	926
Interest paid to IMF	92	261	594	661	778	840	700	700
	(In per cent)							
Debt outstanding/GDP	30.1	35.3	45.7	50.2	48.8	46.2	39.4	33.6
Debt outstanding/GDP 2/	25.9	24.1	31.5	34.9	36.8	37.0	32.8	29.0
Net drawings/GDP	2.9	12.0	14.4	8.5	4.2	2.4	-2.0	-1.8
Debt service/exports of goods and services	5.1	4.8	4.9	11.6	13.8	12.3	11.3	9.5
Average interest rate 3/	2.7	2.7	3.3	5.0	4.6	4.6	4.2	3.7
Debt outstanding (growth rate)	17.6	36.2	38.7	20.5	9.5	5.4	-4.7	-5.2
Debt outstanding (growth rate) 2/	21.8	7.9	40.0	21.8	18.6	12.0	-1.1	-1.3

Source: Fund staff estimates.

1/ Includes IMF and government-guaranteed debt.
2/ Excludes IMF debt.
3/ Ratio of total interest payments to debt at beginning of period.

security system; and (e) the application of the bank deposits levy (of 1 per cent on interest paid on time and savings deposits) to the National Commercial Bank. In addition to the new tax package, central government revenue in 1983/84 is expected to receive a boost from (a) the transfer of profits from the External Trade Bureau (in 1982/83 these profits were used to pay off outstanding debts and to accumulate reserves); and (b) higher income tax collections that should accompany the increase in employment and incomes related to the road rehabilitation project. Government has also embarked on a program to increase collections of import and consumption duties. A new customs law has recently been enacted and, with the aid of technical assistance being provided by the UNDP, customs personnel will be trained in new valuation techniques.

A study of Dominica's tax structure conducted in early 1983 by a member of the Fund's panel of fiscal experts recommended a rationalization of the system of consumption duties and the adoption of a simplified ad valorem rate structure that would narrow rate differentials (which now range from 6 per cent to 84 per cent). In line with this recommendation the Government intends to introduce in 1983/84 a three-tier rate schedule which provides for a standard rate of consumption duty of 25 per cent (replacing the existing 18 per cent rate), a reduced rate of 10 per cent, and a higher rate of 40 per cent. The revision, along with the re-examination of tax exemptions, is expected to yield a small increase in tax revenues in 1983/84.

Current expenditure is projected to increase by 10 per cent in 1983/84, remaining at the equivalent of 30 per cent of GDP. Of the programed EC$6 million increase in these expenditures, EC$2 million represents higher interest payments (mainly payment of charges to the Fund) and EC$3 million is earmarked to cover the 10 per cent wage increase which is scheduled to take effect on January 1, 1984. The increase in the wage bill assumes a further reduction in the number of casual workers and continued tight controls on employment in the central government establishment. Nonwage current spending is expected to be cut back in real terms in all areas except for allocations to cover the higher cost of utilities and for road maintenance under the terms of a loan signed with the International Development Association (IDA).

The authorities had indicated that the very high level of taxation on imports had led to a marked increase in smuggling in the last year or so. In view of this fact and the already high tax ratio (tax revenue represented 26 per cent of GDP in 1982/83), the staff suggested that more of the fiscal adjustment be effected through a curtailment of the wage bill, which represents close to 60 per cent of total current expenditures. The authorities agreed that the reduction in inflation and the increase in income tax allowances granted in 1982/83 justified a reduction in the scheduled wage increase, but were reluctant to press for a revision of the existing wage contract at the present time. However, they indicated that if the revenue performance began to lag behind projections, a reduction in the wage bill would have to be considered in order to ensure the attainment of the fiscal targets.

Central government capital outlays are projected to rise sharply in 1983/84. Disbursements under the multi-donor road project are projected at EC$24 million, equivalent to 57 per cent of investment outlays programed for 1983/84; capital expenditure on agricultural diversification is projected at EC$9 million and on the construction of factory shells at EC$4 million. The authorities explained that many projects which were included in the investment program approved by the IBRD have had to be delayed or postponed because of a shortage of local currency financing. They planned to speed up implementation of these projects if the budgetary assistance from U.S. AID turned out to be greater than projected. Capital outlays in the rest of the public sector are projected at EC$5 million in 1983/84, consisting of ongoing work on the rehabilitation of the Port and of boxing plants of the DBGA (Table 7).

2. <u>Rest of the public sector</u>

With regard to the finances of the public enterprises, the Dominica authorities stated that further adjustment measures as well as restructuring of certain enterprises were needed in order to put the sector on a sound financial basis.

The continuing weak financial position of the Port Authority reflected the low tonnage being handled, the large work force, and the high debt service. To improve the Port's finances, user charges are to be increased by 17-1/2 per cent effective July 1983, and the increase in the wage bill is to be limited to 5 per cent in 1983. In addition, the Government has approached the CDB with a view to rescheduling loans owed by the Port Authority and has commissioned a study, to be financed by the CDB, to look into ways of increasing the efficiency of port operations. The other major public utility, the Central Water Authority, is expected to generate a small current account surplus after the introduction of a 10 per cent increase in water rates, scheduled to go into effect in July 1983.

The Dominica authorities believe that urgent priority must be given to solving the production and marketing problems of the banana industry. They have therefore decided to implement a reorganization scheme which calls for the phased transfer of boxing plant operations from the DBGA to private farmers and the replacement of the DBGA by a small marketing institution. The plan is expected to reduce production costs, to provide greater returns to farmers, and to stimulate increased production. In support of the proposed strategy, U.S. AID has undertaken to provide technical assistance for boxing plant operations and financial assistance for the purchase of inputs and pesticides.

In the past two years, the Government has taken steps to streamline the public sector. On July 1, 1982 the Housing Development Corporation was abolished and responsibility for administering the housing program was transferred to the Ministry of Home Affairs. This year the Government plans to eliminate the Dominica Marketing Board after transferring its more important functions to the ETB. The merger will make better

Table 7. Dominica: Public Sector Capital Outlays

	1977/78	1978/79	1979/80	1980/81	1981/82	Est. 1982/83	Proj. 1983/84
	(In millions of East Caribbean dollars)						
Total	13.8	14.6	18.5	27.9	39.4	36.4	48.1
Central Government	8.2	10.9	15.5	22.5	23.0	27.5	43.3
Rest of the public sector	5.6	3.7	3.0	5.4	16.4	8.9	4.8
	(In per cent of GDP)						
Total	13.0	12.2	13.7	17.1	20.9	17.8	21.1
Central Government	7.7	9.1	11.5	13.8	12.2	13.5	19.0
Rest of the public sector	5.3	3.1	2.2	3.3	8.7	4.3	2.1

Sources: Ministry of Finance, Trade, and Industry; and Fund staff estimates.

use of available management resources and is expected to result in an improvement in export marketing arrangements. The Commonwealth Development Corporation (CDC) has offered to hand over its 51 per cent stock in the Dominica Electric Company to the Central Government which already owns 49 per cent. The Government has indicated that it is prepared to accept the offer as long as it does not involve giving a government guarantee for existing loans. If arrangements for the takeover are successfully completed, the Government plans to sell the shares to the public.

3. Incomes policy

The civil service wage agreement ratified in 1981 and covering the period 1982-84 represented an important breakthrough inasmuch as (1) the annual 10 per cent award was a marked deceleration from the pace of wage increases in 1979-80 and (2) by eliminating the cost of living compensation it helped break the wage-price spiral. Nevertheless, as discussed earlier, the payment of the agreed salary increases could create strains on the central government finances if there should be some slippage in the projected revenue performance. In view of the prospects for the public finances over the next few years, the authorities have initiated discussions with the civil service trade union on an appropriate wage strategy to take effect when the current contract expires. As stated in the letter of intent, the Government believes that in addition to the lower inflation rate and the tax relief measures, a new wage strategy should specifically take into account the urgent need to generate public sector savings and to avoid raising the already high tax burden.

The civil service wage agreement was also designed to serve as a model for wage awards in the public corporations and in the private sector. While the agreement did result in a deceleration in wage increases, compliance with the 10 per cent guidelines has not been generalized. In the case of some public corporations (notably the Port Authority and the Banana Board), wage increases in excess of the guidelines exacerbated their fiscal problems. A policy of wage restraint in these corporations is being actively pursued for 1983/84. Specifically, the Government has requested that corporations take into consideration their ability to pay when negotiating wage contracts. In any event, the Government has stipulated that wage awards involving statutory bodies and state enterprises may not be finalized without Cabinet approval. As noted above, the wage adjustment in the port will be held to 5 per cent in 1983.

4. Private sector

Since its creation in 1981, the Industrial Development Corporation (IDC) has intensified its efforts to attract foreign investment and to encourage the local private sector (which has traditionally preferred commerce) to engage in manufacturing activity. So far the efforts to attract foreign investment have been relatively more successful. During

1982 two foreign-owned garment industries (with a combined employment of 125 workers and total exports of about US$500,000) were established. At least three new more industries (a glove manufacturing operation, a wood processing plant, and a spring water bottling plant) are scheduled to commence operations this year. New locally owned industries that should come on stream either in 1983 or 1984 include a sawmilling and wood drying complex and a lime plant. In addition, the Dominica Coconut Products, the island's largest manufacturing concern, which now specializes in soap, is planning to diversify its operations.

The authorities explained that the major constraint to the expansion of the manufacturing base is the lack of suitable factory space. The IDC presently controls 27,000 square feet of factory space which is fully occupied and another 66,000 square feet is being constructed with the aid of funding from the CDB and OPEC. However, demand for factory space is estimated to be twice the area presently under construction. The IDC would like to be in a position to satisfy this demand and has some spare capacity, and is presently seeking financial assistance for a construction program. Other noted impediments are the inadequacy of the road network and aircargo facilities. The Agricultural and Industrial Credit Bank (AID) was established in 1981 to provide credit facilities for the agricultural and manufacturing sectors. The institution is, however, undercapitalized and is now negotiating with various international financial institutions for funds.

5. Monetary and exchange rate policies

The fiscal targets for 1983/84 imply no net increase in commercial bank borrowing by the Central Government and only a modest increase in credit to the rest of the public sector. The credit program thus leaves room for around 15 per cent of credit expansion for the private sector. The Government has requested that the commercial banks continue to maintain tight conditions on credit for the purchase of automobiles and for consumer durables and to give preference to loans to the manufacturing sector.

Interest rates in Dominica are set by the commercial banks. Deposit rates--which since 1980 have ranged from 3 to 7 per cent--are presently lower than rates prevailing in the more developed countries in the CARICOM region, though more or less in line with the domestic rate of inflation. Rates on commercial bank loans range from a prime rate of 9-1/2 per cent to 13-1/2 per cent for consumer loans. The latter was increased by 1 percentage point last year.

The authorities noted that while commercial banks are now very liquid, they continue to be reluctant to make loans to small-scale manufacturing industries, preferring instead the distributive trades and consumer lending. They were also concerned about the large spread between interest rates charged and paid by commercial banks. The banks have explained that the margins were required to compensate for (a) the 1 per cent government tax on time and savings deposits; and (b) the higher costs of administering a number of small loans. The authorities hoped that more active competition between banks would help to reduce the spread.

The real trade-weighted exchange rate of Dominica appreciated by close to 22 per cent since the end of 1979 (Chart 1). The authorities considered that the appreciation of the East Caribbean dollar had compounded the difficulties of Dominica's export sector, particularly bananas and tourism. However, the parity of the East Caribbean dollar could only be modified by unanimous consent of the member countries. The issue of the level and the peg of the East Caribbean dollar is now being studied by ECCA and is scheduled to be referred to the Council of Ministers of the Organization of East Caribbean States (OECS) later this year.

6. Performance criteria

The financial program contains as performance criteria quarterly ceilings on the Central Government's access to nonconcessionary financing which is defined to cover foreign commercial loans, purchases from the Fund and ECCA,and all loans from domestic sources. Drawdowns of EC$5 million of foreign concessionary loans and grants earmarked for specific projects but now on deposit in commercial banks are also included under the quarterly ceilings. The program contains the usual provisions relating to exchange and trade restrictions and multiple currency practices, and provides for consultation to develop remedial measures if it should appear that the objectives of the program are not being met.

V. Staff Appraisal

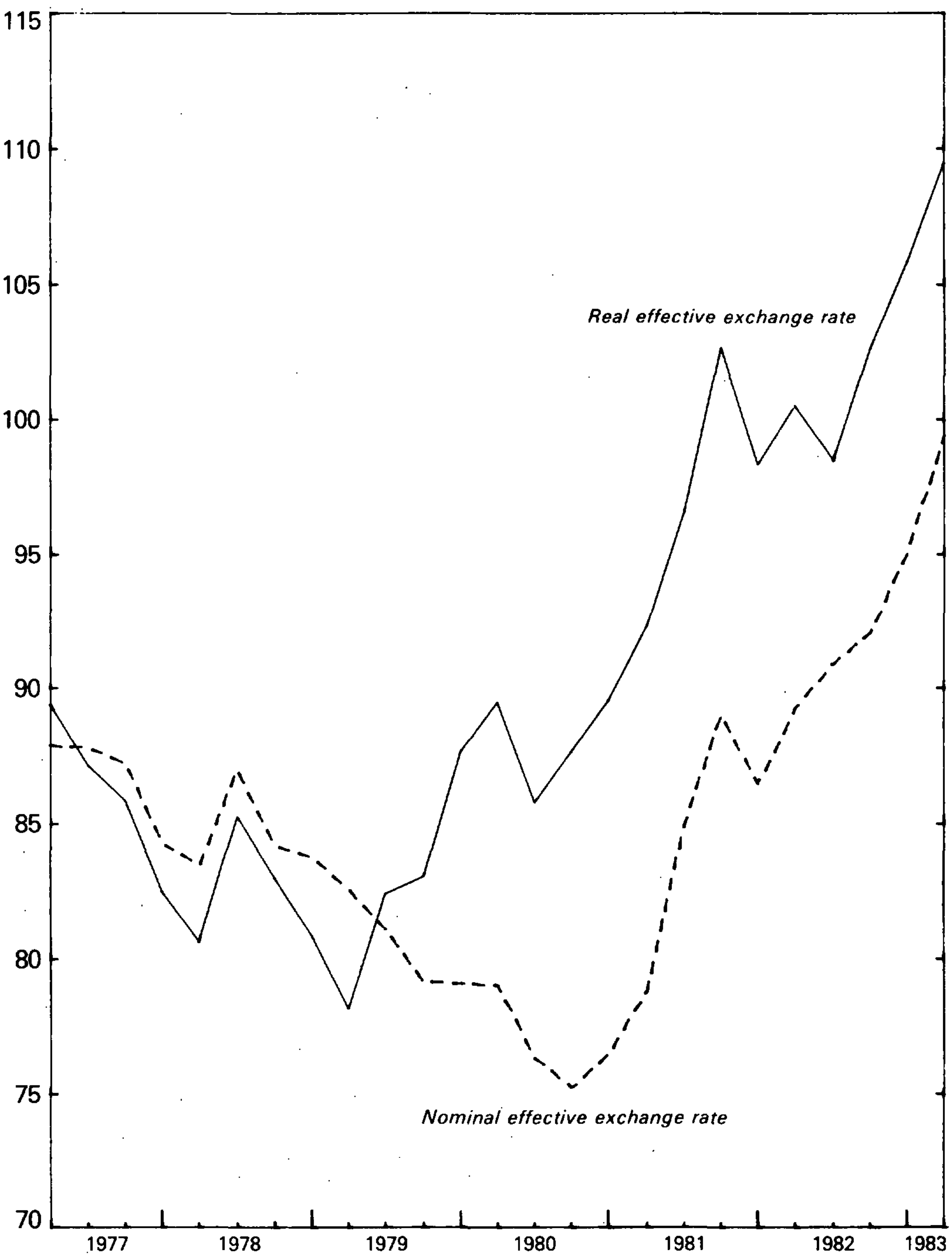
In 1981 Dominica embarked on an EFF program which was to serve as a framework for its recovery effort following the heavy damage caused by hurricanes in 1979 and 1980. The major aims of the program were a structural improvement in the public finances and an expansion of public investment based on concessionary aid flows. The public sector investment program was designed to strengthen Dominica's balance of payments position in the medium term.

Economic developments under the program have been satisfactory. Real GDP rose by 8 per cent in 1981 and 3 per cent in 1982, and the rate of domestic inflation decelerated from 30 per cent in 1980 to 4 per cent in 1982. The deficit on central government current operations was reduced from 18 per cent of GDP in 1979/80 to less than 2 per cent of GDP in 1982/83 and the overall deficit (before grants and concessionary loans) fell from 30 per cent to 15 per cent of GDP. Public investment outlays increased markedly over the period, although they fell short of program levels because of problems of project preparation and implementation and delays in finalizing arrangements for a major road program.

CHART 1

DOMINICA

EFFECTIVE EXCHANGE RATES



Nonconcessionary financing of the budget deficit fell from an average of 6 per cent of GDP in 1980/81 and 1981/82 to 1 per cent of GDP in 1982/83. There was a major improvement in the finances of the public enterprises which reduced their dependence on budgetary support. In the balance of payments the current account deficit was reduced from 56 per cent of GDP in 1980 to 19 per cent of GDP in 1982 and is projected to decline to 16 per cent of GDP by 1984. Dominica has made all the purchases available under the extended arrangement so far.

The program for 1983/84 aims at achieving a balance on the current operations of the Central Government; the overall deficit (before grants and concessionary loans) is, however, projected to increase to 19 per cent of GDP because of a large increase in capital outlays for the ongoing road program. The overall deficit is to be almost entirely financed by concessionary loans and grants. The program is also intended to achieve a further improvement in the finances of the rest of the public sector through an upward adjustment in user charges and the reorganization of the Banana Board.

The fiscal outcome for 1983/84 is predicated on new revenue measures which are expected to raise domestic revenue by the equivalent of 1.3 per cent of GDP to the equivalent of 30 per cent of GDP. Though it might have been preferable that more of the fiscal adjustment be effected through a reduction in the Central Government's wage bill, the staff understands the difficulty of modifying the existing public sector wage contract. However, the authorities will consider a modification of the existing wage contract (the next increase is due in January 1984) or take other measures if government revenue lags behind projections. In respect of the public enterprises the staff recommends that steps be taken to reduce the wage costs of the Port Authority and strongly urges the authorities to speed up the proposed reorganization of the banana industry. Increased producer prices would stimulate higher production levels and complement ongoing efforts at economic diversification.

Efforts to attract foreign investment have now begun to show positive results and a moderate expansion of the manufacturing sector could be expected in the next few years. Dominica's ability to attract foreign investment will be further enhanced by an improvement in its economic infrastructure, particularly the road network and the power generation facilities, and by a continuation of wage restraint and harmonious industrial relations. Wage restraint is of particular importance in the light of the recent appreciation of the East Caribbean dollar on a trade-weighted basis.

For the next few years, Dominica will continue to require external assistance on concessionary terms to assist in the financing of large outlays required for the development of its infrastructural facilities. At the same time, Dominica will need to make further adjustments in demand management so as to increase the level of domestic savings. This will require restraint in the growth of the wage bill of the Central Government and additional measures to increase the profitability of the public enterprises. The staff also urges the Dominica Government to press its regional partners for an early re-examination of the exchange rate policy in the East Caribbean area.

It is recommended that the next Article IV consultation with Dominica be held on the standard 12-month cycle.

VI. Proposed Decision

The following draft decision is proposed for adoption by the Executive Board in concluding the 1983 consultation with Dominica:

Review Under Extended Arrangement

1. Dominica has consulted the Fund in accordance with paragraph 3(b) of the extended arrangement for Dominica (EBS/81/12, Supp. 1, February 9, 1981) and paragraph 15 of the letter dated June 17, 1982, attached thereto, in order to reach understanding with the Fund regarding policies and measures that Dominica will pursue and to establish performance criteria subject to which purchases may be made by Dominica during the remaining period of the EFF arrangement.

2. The letter dated June 3, 1983 from the Prime Minister and Minister of Finance, Trade and External Affairs of Dominica shall be attached to the extended arrangement for Dominica (EBS/81/12, Supp. 1, February 9, 1981) and the letters dated December 5, 1980, July 20, 1981, and June 17, 1982 shall be read as supplemented and modified by the letter dated June 3, 1983.

3. Accordingly, Dominica will not make purchases under this extended arrangement:

(a) during any period after July 1, 1983 in which the data at the end of the preceding period indicate that the limit on the overall budget deficit specified in paragraph 14 of the attached letter dated June 17, 1982 and paragraph 15 of the attached letter of June 3, 1983, is not observed.

4. Purchases under the extended arrangement shall not, without the consent of the Fund, exceed the equivalent of SDR 7,120,000 until August 15, 1983; the equivalent of SDR 7,597,000 until November 15, 1983; and the equivalent of SDR 8,074,000 until January 15, 1984.

Fund Relations with Dominica

Membership date: December 12, 1978.

Status: Article VIII as from December 1979.

Quota: SDR 2.9 million.

Fund holdings of Dominica currency:

As of May 31, 1983	Millions of SDRs	Per Cent of Quota
Total	13.53	446.5
Of which:		
credit tranches	0.73	25.0
compensatory financing	2.78	95.9
extended facility	3.56	122.8
supplementary facility under extended facility	3.56	122.8

SDR Department:

As of March 31, 1983	Millions of SDRs	Per Cent of Cumulative Allocation
Net cumulative allocation	0.592	100.0
Holdings	0.010	1.8

Exchange Rate: EC$2.70 per U.S. dollar.

Recent contacts: An extended arrangement for SDR 8.55 million was approved by the Executive Board on February 6, 1981. The program for the second year of the extended arrangement was approved by the Executive Board on August 2, 1982. Mr. Crawford Reid, a fiscal accounting expert, began a one-year assignment as accounting advisor in June 1981: his appointment has been extended through June 1983. Mr. Stephens, Fund Regional Advisor, has been accredited to Dominica since January 1982. An FAD staff technical assistance mission visited Roseau in October 1982 to review the tax system and to identify additional sources of revenue. A tax consultant was assigned for two weeks in April 1983 to Dominica to help establish an appropriate tax structure.

Dominica--Basic Data

Area and population	
Area	300 sq. miles (790 sq. kilometers)
Population (1982)	80,000
Average annual rate of population increase (1970-81)	1.0 per cent
Unemployment rate (end-1981 estimate)	15-20 per cent
GDP (1982)	SDR 65.1 million
GDP per capita (1982)	SDR 813.8
Origin of GDP	(per cent)
Agriculture and fishing	30.8
Manufacturing	7.2
Construction	8.5
Transport and communications	8.0
Government services	24.3
Other services	21.2
Ratios to GDP (1982)	
Exports of goods and nonfactor services	39.7
Imports of goods and nonfactor services	67.8
Central government domestic revenues (FY 1982/83)	29.5
Central government current expenditures (FY 1982/83)	29.6
External public and government-guaranteed debt (end of year)	31.5
External public and government-guaranteed debt (end of year) 1/	45.7
Gross domestic savings	0.2
Gross investment 2/	28.3
Money and quasi-money (end of year)	36.6

Annual changes in selected economic indicators	1979	1980	1981	1982
		(per cent)		
Real GDP per capita	-18.0	15.8	6.9	2.2
Real GDP	-17.2	17.0	8.0	3.3
GDP at current prices	-6.5	38.6	16.3	7.0
Domestic expenditure (at current prices)	25.6	42.3	-4.0	-3.6
Gross fixed investment 2/	49.0	93.3	-28.0	-10.8
Consumption	20.1	26.2	7.1	-1.6
GDP deflator	20.6	16.1	0.1	2.7
Consumer prices (annual averages)	19.9	29.8	13.9	4.4

	1979/80	1980/81	1981/82	1982/83
Central government domestic revenues (fiscal year July/June)	22.6	52.4	18.1	1.9
Central government current expenditures (fiscal year July/June)	71.0	16.0	-4.6	-1.3
Money and quasi-money	38.0	-9.8	8.4	17.7
Money	52.1	-37.0	19.3	2.2
Quasi-money	32.3	0.6	5.8	21.8
Net domestic assets 3/	-1.8	14.2	27.9	1.2
Credit to public sector (net)	8.4	-0.9	-1.4	-3.0
Credit to private sector	8.0	11.7	26.0	3.4
Merchandise exports, f.o.b.	-40.9	3.2	96.9	28.3
Merchandise imports, c.i.f.	38.2 4/	35.0 4/	-6.6	-4.4
Travel receipts (gross)	-16.1	11.5	10.3	25.0

Central government finances 5/	1979/80	1980/81	1981/82	1982/83
	(millions of East Caribbean dollars)			
Domestic revenue	31.5	48.0	56.7	57.8
Total expenditures	71.6	87.6	85.1	88.8
Current account surplus or deficit (-) before grants	-24.6	-17.1	-5.4	-3.5
Overall surplus or deficit (-)	-40.1	-39.6	-28.4	-31.0
Foreign grants	34.2	27.5	12.1	13.7
Foreign financing (net)	0.3	2.3	3.8	15.0
Change in Government's foreign assets	-0.1	-2.0	0.1	-0.6
IMF 6/	7.3	9.5	8.4	8.4
ECCA	0.6	2.0	--	--
Domestic financing (net) and residual	-2.2	0.3	4.0	-5.5

Balance of payments	1979	1980	1981	1982
	(millions of U.S. dollars)			
Merchandise exports (f.o.b.)	9.4	9.7	19.1	24.5
Merchandise imports (c.i.f.)	-39.4 4/	-53.2 4/	-49.7	-47.5
Travel (net)	1.7	1.7	2.2	3.0
Other services	-0.1	0.3	0.6	-0.3
Private transfers (net)	13.7	10.0	6.2	7.0
Balance on current account	-14.7	-32.5	-21.6	-13.3
Official capital and transfers (net)	21.3	19.2	14.1	13.1
Private capital (net) 7/	-10.1	13.5	2.0	-2.8
SDR allocation	0.3	0.3	0.3	--
Overall surplus or deficit (-)	-3.2	0.5	-5.2	-3.0

1/ Including IMF debt.
2/ Includes rehabilitation outlays.
3/ Changes in relation to the liabilities to the private sector at the beginning of the year. Excludes contra-entry for SDR allocations.
4/ Includes relief imports estimated at US$10 million in 1979 and US$5.6 million in 1980.
5/ Refers to fiscal year beginning July 1.
6/ Includes SDR allocation of EC$0.7 million each in 1979, 1980, and 1981.
7/ Includes errors and omissions.

Dominica: Selected Economic and Financial Indicators, 1980-83

	Actual 1980	1981 Prog.	1981 Actual	1982 Prog.	1982 Actual	Est. 1983
	(Annual per cent changes, unless otherwise specified)					
National income and prices						
GDP at constant prices	17.0	8.5	8.0	2.8	3.3	5.3
GDP deflator	16.1	10.6	0.1	6.5	2.7	4.0
Consumer prices	29.8	14.0	13.9	6.5	4.4	6.0
External sector (on the basis of U.S. dollars)						
Exports, f.o.b.	3.2	111.3	96.9	0.5	28.3	7.3
Imports, c.i.f.	35.0	-3.0	-6.6	-4.7	-4.4	5.7
Non-oil imports, c.i.f.	28.9	...	-6.8	-4.7	-4.1	11.7
Export volume	-18.1	133.3	104.7	4.0	17.2	12.2
Import volume	-9.1	7.7	2.8	-7.0	-7.9	2.6
Terms of trade (deterioration -)	-6.6	-6.4	-3.2	--	7.3	-2.0
Nominal effective exchange rate (depreciation -)	-5.1	--	9.1	--	8.7	--
Real effective exchange rate (depreciation -)	6.1	...	10.4	--	4.3	--
Money and credit						
Domestic credit (net) 1/	14.2	15.6	25.4	10.2	-3.1	2.5
Public sector	-2.8	--	4.5	--	-3.6	0.1
Private sector	13.5	15.6	23.9	10.2	-0.2	3.4
Money and quasi-money (M-2)	-9.7	9.0	4.8	9.5	17.3	17.0
Velocity (GDP relative to M-2)	2.2	2.6	2.5	2.3	2.7	2.6
Interest rate (three-month time deposit)	4.0	...	4.5	4.5	4.5	4.5
	(In per cent of GDP)					
Gross domestic investment	54.4	...	33.7	30.8	28.3	29.9
Gross domestic savings	-17.8	...	-8.5	-6.8	0.2	4.1
Current account deficit (BOP)	-56.1	-26.0	-32.1	-28.8	-18.5	-17.7
External debt						
Inclusive of use of Fund credit	30.1	42.0	35.3	41.5	45.7	50.2
Debt service as a per cent of exports and service receipts	5.1	4.5	4.8	4.5	4.9	11.6
Interest payments (in per cent of exports of goods and services)	3.2	4.4	2.1	4.4	2.7	5.4
	(In millions of SDRs, unless otherwise specified)					
Overall balance of payments	0.4	-4.4	-5.2	-3.3	-2.5	-2.0
Gross official reserves (months of imports) 2/	--	--	--	--	--	--
External payments arrears	--	--	--	--	--	--
	FY 1980/81	FY 1981/82		FY 1982/83		1983/84 Program
	(Annual per cent changes, unless otherwise specified)					
Government budget						
Domestic revenue	52.4	15.4	18.1	6.9	1.9	15.9
Total expenditure and net lending	22.3	7.8	-2.8	21.4	4.3	24.4
	(In per cent of fiscal year GDP)					
Central government savings	-10.5	-2.8	-2.9	-0.3	-1.7	-0.1
Central government budget deficit (overall) 3/	-24.3	-20.9	-15.3	-21.1	-15.2	-19.2
Foreign grants and concessionary loans	18.0	14.3	8.5	17.0	14.1	16.7
Financing requirement (including IMF)	6.3	4.9	6.8	4.1	1.1	0.3 4/
Of which: domestic bank financing	-0.5	--	2.3	--	--	--

1/ In relation to liabilities to private sector at beginning of period.
2/ Because of its membership in ECCA, Dominica does not hold foreign reserves, except for small balances of sinking funds for debt repayments.
3/ Excluding transfers.
4/ Excludes the drawdown on earmarked deposits.

Summary of Financial Program for FY 1983/84

1. Principal assumptions

(a) Growth in real GDP of 5-1/2 per cent in 1983 and 7 per cent in 1984.

(b) An average annual increase in the consumer price index of 6 per cent and the GDP deflator of 4 per cent in 1983-84.

2. Targets

(a) Central government operations are projected to show a current account deficit of EC$0.2 million in 1983/84 and an overall deficit (before grants and foreign concessionary loans) of EC$43.5 million (19 per cent of GDP). The overall deficit is projected to be almost entirely financed by grants and concessionary loans.

(b) The current account deficit of the balance of payments is projected at US$14 million (18 per cent of GDP) in 1983; the current account deficit is expected to be reduced to the equivalent of 16 per cent of GDP in 1984.

3. Major elements of the program

(a) Revenue measures

The program provides for a tax package (estimated to yield EC$2.9 million) containing the following measures, all of which take effect as of July 1, 1983:

(i) Introduction of customs tariff on imports of the External Trade Bureau--mainly sugar and rice--(EC$0.2 million).

(ii) Increase in the foreign exchange tax from 1 per cent to 1.5 per cent (EC$0.6 million).

(iii) Imposition of hospital fees and charges (EC$0.5 million).

(iv) Increase in consumption duties on fuels (EC$0.5 million).

(v) Extension of the bank deposits levy to the National Commercial Bank (EC$0.3 million).

(vi) Transfer of profits of the External Trade Bureau (EC$0.8 million).

(b) Expenditure measures

(i) Limiting current spending of the Central Government to EC$67.2 million representing an increase of EC$5.9 million (9.6 per cent) over the estimated level of 1982/83.

(ii) Central government capital expenditures in 1983/84 have been programed at EC$43.3 million. The main sources of finance for these expenditures are (a) foreign project grants of EC$23.6 million; (b) foreign budgetary grants of EC$3.5 million; (c) foreign concessionary loans in an amount of EC$10.7 million; and (d) drawdowns of EC$5 million from balance of payments loans received in 1982 but now on deposit at commercial banks.

(c) Public enterprises

(i) A reorganization plan for the banana industry is to be initiated in 1983/84. The plan involves a phased transfer of boxing plant operations from the Dominica Banana Growers' Association (DBGA) to the private banana growers and the establishment of a small institution to concentrate exclusively on marketing activities.

(ii) Port charges will be increased by 17-1/2 per cent effective July 1, 1983.

(iii) Water rates will be increased by 10 per cent effective July 1, 1983.

(d) Other policies

(i) The wage guideline for 1983/84 is an increase of 10 per cent, the size of the wage adjustment for central government workers that takes effect on January 1, 1984.

(ii) The existing restrictions on commercial banks' credit expansion for the purchase of motor cars and consumer durables are to remain. Also, no increase in bank credit to the Central Government (except the drawdown of earmarked deposits referred to above) is programed in 1983/84.

(e) Performance criteria

Cumulative quantitative limits on central government budget financing defined as the sum of any SDR allocation, the net use of foreign resources, net borrowing from ECCA, net use of foreign assets, net borrowing from foreign commercial and net borrowing from domestic sources (including drawdowns of the earmarked resources referred to above) have been set as follows:

July 1, 1983 - September 30, 1983:	EC$2.2 million
October 1, 1983 - December 31, 1983:	EC$5.1 million
January 1, 1984 - March 31, 1984:	EC$5.2 million.

Roseau, Dominica, W.I.
June 3, 1983

Mr. Jacques de Larosière
Managing Director
International Monetary Fund
Washington, D.C. 20431
U.S.A.

Dear Mr. de Larosière:

1. In 1981, the Government of Dominica embarked upon a program to reconstruct the economy which was devastated by hurricanes in 1979 and 1980 and by years of social and political instability. The extended arrangement with the IMF, which was to provide a framework for the recovery effort, aimed specifically at (a) strengthening the public sector finances, (b) promoting higher levels of public sector investment and foreign aid and (c) reorienting the investment effort in a manner that would strengthen the balance of payments position in the medium term. The fiscal program envisaged that with the aid of various revenue measures and, more so, by controlling operating expenditures, the current operations of the Central Government would be shifted from a deficit equivalent to 18 per cent of GDP in 1979/80 to equilibrium in 1983/84. With the assistance of the IBRD, the Government formulated a three-year investment program which focused on (a) the restoration and improvement of infrastructure damaged by hurricanes, (b) the diversification of agricultural production and (c) the expansion and diversification of the manufacturing sector. This investment program envisaged an increase in the annual level of capital outlays from the equivalent of 12 per cent of GDP in 1979/80 to 22 per cent of GDP in 1982/83. The bulk of these outlays were earmarked to be financed by foreign grants and concessionary loans. Nonconcessionary financing of the budget deficit was to be progressively reduced from the equivalent of 8 per cent of GDP in 1980/81 to 4 per cent of GDP in 1982/83 and be virtually eliminated in 1983/84.

2. We have made steady progress with our recovery program. The hurricane damage resulted in a fall in real GDP of 18 per cent in 1979, but the rapid recovery in banana production combined with a strong expansion in domestic agriculture and manufacturing, led to an average annual growth of real GDP of 12 per cent in 1980-81. The increase in real GDP decelerated to 3 per cent in 1982, reflecting a slower growth of output in agriculture, construction and the distributive trades. The annual rate of inflation fell steadily from 30 per cent in 1980 to 4 per cent in 1982 and the current account deficit of the balance of payments was more than halved from US$33 million (56 per cent of GDP) in 1980 to US$13 million (19 per cent of GDP) in 1982. The improvement in the public finances from 1980 to 1982 also was impressive. Much of what has been accomplished in the last two and one-half years is attributable to the marked improvement in the climate of industrial relations and the sense of responsibility displayed by our trade unions in restraining wage demands.

3. The process of recovery is, however, still far from complete. In 1982, output of bananas was about 23 per cent below the prehurricane level and the number of tourist arrivals, 10 per cent lower than in 1978. Dominica's banana industry is now facing acute financial difficulties due to the cumulative impact of low productivity, inefficient organization, continuously rising costs and more recently, the depreciation of the pound sterling vis-à-vis the East Caribbean dollar. The expansion of domestic agricultural output continues to be constrained by transport and marketing difficulties, and the inflow of foreign investment in the manufacturing sector has been much slower than originally anticipated.

4. The economic program for 1983/84 will aim at consolidating the gains made over the last two years and removing the constraints which impede production in the major sectors. Emphasis will be placed on promoting further adjustment in the public finances and improving the rate of implementation of the investment program. Economic policy will also stress the promotion of conditions favorable to the development of private initiative and the attraction of foreign private investment.

Public finances

5. In 1980/81 and 1981/82, the Central Government succeeded in reducing the current account deficit to EC$17.1 million (10.5 per cent of GDP) and EC$5.4 million (2.9 per cent of GDP) respectively. This reduction was almost exactly in line with the original targets of the program. Over these two fiscal years, domestic revenue rose by 80 per cent while the growth in current expenditure was held to 11 per cent. The expenditure restraint was facilitated by the elimination of transfers to the Dominica Banana Growers' Association (DBGA) and the substantial tariff adjustment in the Port and Water Authorities which eliminated the need for budgetary support. In 1980/81, central government investment outlays exceeded program targets. However, in 1981/82, delays in the disbursement of concessionary assistance adversely affected the implementation of the investment program and the planned increase in capital outlays was not achieved. In both years, the Central Government's use of nonconcessionary financing declined as envisaged in the program.

6. In 1982/83, the current account deficit on central government operations turned out to be EC$3.5 million compared with a programed deficit of EC$0.7 million. Government revenues fell below projected levels because of a fall in taxable imports and delays in the imposition of hospital fees and charges. Central government current expenditures were held to the levels envisaged in the program as larger than budgeted interest payments were offset by savings in other expenditure categories. Capital outlays had to be cut back below program levels because of delays in finalizing arrangements for a major road rehabilitation project. The Central Government's recourse to nonconcessionary financing was, however, kept within program limits because of the receipt of special budgetary assistance from the European Development Fund (to compensate for shortfalls on coconut exports) and the OPEC Special Fund.

7. The fiscal plan for 1983/84 incorporates revenue and expenditure measures projected to bring the Central Government's current operations into virtual balance. When allowance is made for commodity assistance expected from U.S. AID, the current operations of Central Government are projected to show a surplus of EC$3.3 million.

In 1982/83, with the aid of technical assistance provided by the International Monetary Fund, the Government undertook a review of the system of indirect taxation. As a result of this review, the following changes are to be introduced in the budget for 1983/84:

(a) Imports of the External Trade Bureau (ETB) will now begin to be subject to customs tariffs. In addition, the ETB will be required to transfer part of its operating surplus to the Central Government.

(b) Consumption duty rates which now range from 6 per cent to 84 per cent are to be rationalized and consolidated into fewer categories. The reorganization, whose principal objective is to simplify the present structure of consumption duties, is also expected to yield a small increase in government revenue.

(c) During FY 1982/83, in line with the fall of import prices, the retail price of gasoline was reduced from EC$6.15 per gallon to EC$5.50 per gallon; the retail price of kerosene from EC$4.25 per gallon to EC$4.00 per gallon and diesel from EC$4.50 per gallon to EC$4.40 per gallon. As a result of subsequent adjustments in landed costs, and the Government's weak fiscal situation, prices are to be reset at EC$6.00 per gallon for gasoline, EC$4.20 per gallon for kerosene and EC$4.50 per gallon for diesel.

(d) The introduction of hospital fees and charges that was announced in the 1982/83 budget but not implemented because of administrative problems will take effect on July 1, 1983.

(e) The tax on the sale of foreign exchange will be increased from 1 per cent to 1.5 per cent.

(f) Existing legislation will be revised to make the bank deposits levy applicable to deposits of the National Commercial Bank.

These revenue measures have been estimated to yield EC$2.9 million. In addition, nontax revenue will increase by EC$3.5 million representing proceeds of the sale of commodities provided as a grant by U.S. AID.

8. Current expenditure in 1983/84 is to be held to a level of EC$67.2 million, EC$5.9 million (10 per cent) over 1982/83; EC$2 million of the increase represents higher interest payments (including the payment of charges to the Fund); EC$3 million represents the increase in the wage bill to finance the final phase of the wage award granted in 1980. The budgetary allocation for wages and salaries assumes no increase in the size of the civil service establishment and a small

reduction in the number of casual workers. With the cash management techniques introduced last year, the Government intends to limit the increase in nonwage operating expenditures to EC$1 million. This allocation has been specifically made to cover the higher cost of utilities and increased commitments for road maintenance under the terms of the IBRD road program.

9. The civil service agreement which established a 10 per cent annual increase for the period 1982-84 represented a marked moderation from the earlier pattern of wage settlements. However, because of the absolute size of the wage bill (which accounts for about 58 per cent of total current expenditures) and the sluggish revenue performance over the past year, payment of the agreed salary increases created severe strains on the Central Government's finances in 1982/83. The Government has begun discussions with the civil service union on an appropriate wage policy to take effect when the current contract expires. The new strategy will take into account (a) the urgent need to generate public sector savings, (b) the already high tax burden and (c) the sharp reduction in the domestic rate of inflation and the income tax relief provided in 1983.

Public investment program

10. Public sector investment outlays for 1983/84 are projected at EC$48.1 million; EC$43.3 million programed to be spent by the Central Government and EC$4.8 million by the state enterprises. The four-year multi-donor road project, which began but proceeded very slowly in 1982/83 because of administrative bottlenecks, will get into full gear in 1983/84. This project is of particular importance to the economic recovery effort as the poor state of the road network has become a severe constraint on productive activity. Expenditure on the road program for 1983/84 has been projected at EC$25.0 million; capital outlays on agricultural development are projected at EC$8.4 million and on the construction of factory shells at EC$4.2 million.

11. Over 80 per cent of programed central government investment outlays is to be financed from external grants and concessionary loans; external grants are projected at EC$23.6 million (comprising U.S. AID, EC$7 million, CIDA, EC$10.3 million, EDF, EC$2.8 million and BDD, EC$3.2 million) while net disbursements on concessionary loans, mainly from the IDA and CDB, are projected at EC$10.7 million. The latter figure excludes EC$5.0 million, representing proceeds of foreign concessionary loans and grants received in 1982/83 but now deposited at the National Commercial Bank. These proceeds, which are earmarked for specific capital projects, are expected to be drawn down during 1983/84.

Public enterprises

12. In 1983/84, the Government intends to intensify its efforts to improve the medium-term viability of the main public enterprises. Even after reducing producer prices to uneconomic levels, and rescheduling debt service obligations, DBGA registered an operating deficit of

EC$1.6 million in 1982/83. During this fiscal year, the Government intends to initiate a medium-term rationalization program which would provide for a phased transfer of boxing plant operations to private farmers and the transformation of the Board into a small efficient marketing agency run along strict business lines. The program will receive technical assistance from U.S. AID which will also make available US$1.3 million for the purchase of spray oil and fungicide for leaf spot control. The operations of the Port Authority in 1982/83 yielded a current account deficit of EC$1.0 million. The Authority also experienced severe difficulties in meeting debt service payments. The poor state of the Authority's finances reflected the low tonnage being handled, the high debt service burden and escalating wage costs. To improve the finances, port charges are to be increased by 17 per cent effective July 1983 and a freeze on the wages of a significant part of the work-force in respect of 1983 was implemented. Government has approached the Caribbean Development Bank (CDB) with a view to rescheduling outstanding loans owed by the Port Authority and has commissioned a study, financed by CDB, to look into ways of increasing the efficiency of port operations. The Government is committed to adopt whatever measures are necessary to have the Port operate on a self-financing basis as soon as possible. The Central Water Authority is expected to generate a current surplus in 1983/84 with the aid of a 10 per cent increase in water rates. The Government has decided to eliminate the Dominica Marketing Board after a transfer of its more important functions to ETB. The merger will reduce operating costs and will make optimum use of available management resources.

Other policies

13. The civil service wage agreement was designed to serve as a guideline for wage awards in the rest of the economy. While this guideline undoubtedly helped to moderate the pace of wage increases, compliance has not been generalized. In a few instances, wage increases in excess of the guidelines have served to exacerbate the weak financial position of certain state enterprises. The Government is committed to secure wage restraint in order to facilitate improvement in the public finances, prevent a further decline in traditional export activities and create better conditions for private investment. The Government will continue its dialogue with the trade unions and employers in its effort to obtain support for the observance of the wage guidelines. Statutory bodies and state enterprises will be required to take into consideration their ability to pay when negotiating wage contracts. In any event, Government intends to stipulate that before wage negotiations are finalized by statutory bodies and state enterprises, approval of the Cabinet must be obtained.

14. Government would like the banking system to adopt a structure of interest rates which would better promote the accumulation of savings and help in allocating credit more efficiently. This objective will be pursued within the context of a coordinated regional interest rate strategy to be developed by the regional central bank soon to be

established. Over the past year, the Government has refrained from borrowing from the domestic banking system and has sought to encourage the commercial banks to tighten credit for motor cars and consumer durables so as to increase credit availability for productive purposes. The Government intends to continue this strategy in 1983/84; during the fiscal year, there will be no net credit expansion to the Central Government and only a modest increase to the public entities. It was hoped that the private sector would take full advantage of the increase in bank liquidity which has already taken place and which is projected to increase even further in 1983/84. Mortgage lending by the Agricultural Industrial and Development Bank is expected to increase markedly in 1983/84 based on resources to be obtained from CDB (EC$3.5 million) with counterpart funding of an equivalent amount provided by the Social Security System.

15. Quantitative limits on the budget financing requirement, defined as the sum of any SDR allocation, the net use of Fund resources, net borrowing from domestic sources (including the earmarked resources referred to in paragraph 11), net borrowing from ECCA, net use of foreign assets and net borrowing from foreign commercial banks, have been set for the period ending February 1984. The cumulative financing requirement shall not exceed EC$2.2 million during the quarter ending September 1983, EC$5.1 million during the quarter ending December 1983 and EC$5.2 million during the quarter ending March 1984.

16. The Government of Dominica reiterates the statements made in paragraph 15 of the letter of December 5, 1980 with regard to exchange and trade restrictions and multiple currency practices.

17. The Government of Dominica believes that the policies set forth in this letter will achieve the objectives of its program but will take any further measures that may be appropriate for this purpose. The Government will consult with the Fund on the adoption of any measures that may be appropriate in accordance with policies of the Fund on such consultations.

18. In spite of the considerable balance of payments adjustment that has taken place in the recent past, an unsustainable current account deficit will still remain for the next one or two years. Accordingly, on the basis of the program outlined above, the Government intends to request additional use of Fund resources following the completion of the current extended arrangement and hopes that the Fund will give favorable consideration to the request.

Sincerely yours,

/s/

M. Eugenia Charles
Prime Minister and Minister of
Finance, Trade and External Affairs