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August 9, 1983

To: Members of the Executive Board

From: The Acting Secretary

Subject: Grenada - Staff Report for the 1983 Article IV Consultation and Request for Extended Arrangement

Attached for consideration by the Executive Directors is the staff report for the 1983 Article IV consultation with Grenada and its request for an extended arrangement equivalent to SDR 13.5 million. Draft decisions appear on page 22.

It is understood that the Executive Director for Grenada will be proposing a date for Executive Board consideration of this matter.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. Sundgren (ext. 73722) or Mr. Hardy (ext. (5)7158).

Att: (1)

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

GRENADA

Staff Report for the 1983 Article IV Consultation and Request for Extended Arrangement

Prepared by the Western Hemisphere Department

(In consultation with the Exchange and Trade Relations, Fiscal Affairs, Legal, and Treasurer's Departments)

Approved by E. Wiesner and W.A. Beveridge

August 9, 1983

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I. Introduction

The Article IV consultation discussions with Grenada were held in St. George's during May 2-25, 1983. At the same time a program was negotiated in support of which Grenada is requesting a three-year extended arrangement from the Fund (see attached letter). Further discussions were held at headquarters in the period July 7-19, 1983. The Grenadian representatives included the Deputy Prime Minister and Minister of Planning, Finance and Trade, the Minister of Tourism and Civil Aviation, other senior government officials and heads of various state enterprises. The mission also held discussions with private entrepreneurs, business associations, and commercial banks. The staff representatives were Messrs. Hardy (Head), Yadav, and Sundgren, Ms. Spinola (all WHD), Mr. Tsukahara (FAD), and Ms. Boyd (Secretary-ETR); the mission was assisted by the Fund's Regional Advisor, Mr. Stephens, stationed in Antigua and by Ms. Buyck, a staff member of the Inter-Agency Resident Mission. Mr. Casey, the Alternate Executive Director for Grenada, participated in the final round of policy discussions.

The last Article IV consultation discussions with Grenada were held in November 1980 and concluded by the Executive Board in May 1981. Grenada continues to avail itself of the transitional arrangements of Article XIV.

The program in support of which the extended arrangement is being requested is described in the attached letter and is analyzed below. The requested extended arrangement is in an amount of SDR 13.5 million (equivalent to 300 per cent of Grenada's present quota of SDR 4.5 million) consisting of SDR 4.525 million of ordinary resources and SDR 8.975 million of borrowed resources. Under the arrangement up to SDR 4.5 million would be available to Grenada in the period through August 15, 1984, and up to SDR 9 million in the period through August 15, 1985. In the period through August 15, 1984, the phasing would be as follows: purchases shall not exceed SDR 1.125 million until November 15, 1983, SDR 2.25 million until February 15, 1984, and SDR 3.375 million until May 15, 1984.

As of June 30, 1983, the Fund's holdings of Grenada's East Caribbean dollars in the credit tranches were SDR 2.9 million, or 64.4 per cent of quota (Appendix A). Taking into account scheduled repurchases, full use of the requested extended arrangement would raise the Fund's holdings of Grenada's currency to SDR 18.225 million, or 405 per cent of quota: of these, holdings under the credit tranche policies would be SDR 13.725 million, or 305 per cent of quota (Table 1).

For about two-and-a-half years the Grenadian authorities have been seeking to negotiate an EFF arrangement with the Fund. Instead, in May 1981 a one-year stand-by arrangement in an amount equivalent to SDR 3.425 million (76 per cent of quota) was negotiated and approved by the Executive Board. All purchases were made except the last one because understandings were not reached on ceilings covering the last few months of the arrangement. During several subsequent contacts the authorities have renewed their request for an EFF arrangement.

Table 1. Grenada: Projection of IMF Position
June 30, 1983-June 30, 1986

	Outstanding June 30 1983	Operations in First Year of Arrangement 1983 July-Sept.	Oct.-Dec.	1984 Jan.-Mar.	Apr.-June	Outstanding June 30 1984	Operations in Second Year 1984/85 July-June	Third Year 1985/86 July-June	Outstanding June 30 1986
	(In thousands of SDRs)								
Purchases	4,300	1,125	1,125	1,125	1,125	8,625	4,500	4,500	13,725
Under tranche policies	2,900	1,125	1,125	1,125	1,125	7,400	4,500	4,500	13,725
Ordinary	(2,900)	(--)	(238)	(563)	(563)	(4,264)	(2,252)	(913)	(4,754)
Borrowed	(--)	(1,125)	(887)	(562)	(562)	(3,136)	(2,248)	(3,587)	(8,971)
Compensatory financing	1,400	--	--	--	--	1,225	--	--	--
Repurchases		--	--	--	175		1,925	1,975	
Under tranche policies		--	--	--	--		1,225	1,450	
Ordinary		(--)	(--)	(--)	(--)		(1,225)	(1,450)	
Compensatory financing		--	--	--	175		700	525	
Net purchases	4,300	1,125	1,125	1,125	950		2,575	2,525	
Memorandum items:									
Total holdings (end of period)	8,800	9,925	11,050	12,175	13,125	13,125	15,700	18,225	18,225
Excluding compensatory	7,400	8,525	9,625	10,775	11,900	11,900	15,175	18,225	18,225
	(In per cent of quota)								
Total holdings (end of period)	195.6	220.6	245.6	270.6	291.7	291.7	348.9	405.0	405.0
Excluding compensatory	164.4	189.4	213.9	239.4	264.4	264.4	337.2	405.0	405.0

Source: International Monetary Fund.

II. Recent Economic Developments

Grenada's recent economic performance has been adversely affected by the world recession and by the effects on tourism of unfavorable publicity abroad. Nevertheless, real GDP grew by about 3 per cent a year over the last four years, led by construction which reflected rising public sector investment (Table 2). Output in agriculture, fisheries, and forestry has shown a stagnant or slightly declining trend over this period: output recovered partially in 1981 from the effects of a hurricane in 1980, but fell again in 1982 as drought affected export crops. Manufacturing production, primarily the processing of agricultural products, recovered in 1981 from declines in the preceding two years, but it had not registered further growth in 1982. There was a 27 per cent decline in stayover tourist arrivals from 1979 to 1982. The growth of output is expected to slow down slightly in the current year, mainly because of a lower rate of expansion of construction although value added in hotels and restaurants is expected to pick up due to a recovery of about 8 per cent in tourist arrivals.

The rate of inflation, measured by changes in the consumer price index, declined from an average of 20 per cent a year in 1980-81 to 7.8 per cent in 1982, and to 5.5 per cent in the 12 months through April 1983. The slowdown reflected mainly lower increases in import prices: this effect was magnified in 1982 by the continued appreciation of the East Caribbean dollar (which is pegged to the U.S. dollar) in relation to many currencies. An improvement in domestic food supplies also helped the price performance last year. Wage increases in 1982 were about 12 per cent compared with around 16 per cent in the preceding year, and are expected to slow further in 1983. The three-year civil service wage agreement of 1981 provided for an increase of 17.3 per cent from January 1981, 10 per cent from January 1982, and 12 per cent from January 1983. The Government has undertaken a campaign to explain the importance of relating wage demands to productivity and to the employer's ability to pay.

The principal feature of the public sector finances since 1978 has been the rapid rise in the fiscal deficit from EC$13 million (7.5 per cent of GDP) in 1979 to EC$97 million (33 per cent of GDP) in 1982, in the main resulting from the very sharp expansion in capital outlays (Table 3). In financing this deficit the authorities relied almost entirely on external grants and foreign concessional loans up to 1980, after which they also utilized significant foreign commercial loans and financing from the domestic banking system. Use of these types of resources rose to almost 13 per cent of GDP in 1982. Commercial foreign borrowing has been mostly in the form of suppliers' credits for the airport equipment.

In the years 1979-82 revenue growth averaged 13.5 per cent a year, approximately in line with the growth of GDP. Revenue performance was helped by discretionary tax measures in both 1981 and 1982. However, boosted by investment spending, expenditure increases far exceeded the

Table 2. Grenada: Indicators of National Accounts and Prices

	1979	1980	1981	1982	Est. 1/ 1982/83	Projected 1/ 1983/84	1984/85	1985/86
	(In millions of East Caribbean dollars)							
Nominal GDP at market prices	202.6	232.2	258.8	290.5	305.9	335.4	368.7	413.5
Real GDP (1980 factor prices)	189.4	195.1	201.7	208.3	211.1	216.0	222.5	233.6
	(Annual percentage change)							
Nominal GDP at market prices	17.6	14.6	11.5	12.2	11.4	9.6	9.9	12.2
Real GDP (1980 factor prices)	2.1	3.0	3.4	3.3	3.0	2.3	3.0	5.0
GDP deflator	14.8	14.4	9.6	7.5	7.3	7.0	7.3	7.7
Consumer price index	20.0	21.2	18.8	7.8	7.5	7.0	6.9	6.8

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

1/ Year beginning July.

Table 3. Grenada: Summary Public Sector Operations

	1979	1980	1981	Prel. 1982	Est. 1/ 1982/83	Program 1/ 1983/84	1984/85	1985/86
	(In millions of East Caribbean dollars)							
Total revenue	55.1	59.0	63.0	75.2	82.9	96.7	110.6	125.3
Current revenue	54.9	58.8	62.7	75.2	82.9	96.7	110.6	125.3
Government	(54.9)	(57.5)	(62.7)	(74.2)	(81.9)	(89.7)	(102.8)	(116.7)
Current surplus of nonfinancial public enterprises	(--)	(1.3)	(--)	(1.0)	(1.0)	(2.0)	(2.3)	(2.6)
Surplus of National Insurance Scheme	(--)	(--)	(--)	(--)	(--)	(5.0)	(5.5)	(6.0)
Capital receipt	0.2	0.2	0.3	--	--	--	--	--
Total expenditure	81.6	98.3	142.5	172.3	182.9	188.9	177.6	192.2
Current expenditure	54.0	59.6	64.6	67.5	73.9	85.0	93.8	101.8
Government	(53.9)	(59.6)	(63.8)	(67.5)	(73.9)	(85.0)	(93.8)	(101.8)
Current deficit of nonfinancial public enterprises	(0.1)	(--)	(0.8)	(--)	(--)	(--)	(--)	(--)
Capital expenditures	27.6	38.7	77.9	104.8	109.0	103.9	83.8	90.4
Of which: airport	(10.1)	(21.0)	(34.3)	(46.2)	(64.6)	(40.0)	(0.4)	(--)
contingency fund	(--)	(--)	(--)	(--)	(--)	(1.0)	(1.7)	(3.3)
Current balance	0.9	-0.8	-1.9	7.7	9.0	11.7	16.8	23.5
Overall balance	-26.5	-39.3	-79.5	-97.1	-100.0	-92.2	-67.0	-66.9
External grants	18.6	34.4	34.9	45.0	45.5	42.1	26.8	31.8 2/
Overall balance after grants	-7.9	-4.9	-44.6	-52.1	-54.5	-50.1	-40.2	-35.1
External concessionary loans (net)	6.4	3.5	19.9	14.7	19.4	26.5	38.3 3/	31.7 3/
Nonconcessional financing	1.5	1.4	24.7	37.4	35.1	23.6	1.9	3.4
Commercial loans (external)	--	--	--	4.4	21.9	16.8	--	--
Change in foreign assets	-0.2	-1.1	2.7	--	--	2.4	--	--
SDR allocation	1.1	1.1	1.1	--	--	--	--	--
Net IMF purchases	1.2	--	15.6	-2.4	-2.0	12.3	6.9	6.3
Net ECCA borrowing	1.0	0.9	2.2	2.2	2.2	--	--	--
Net domestic borrowing	-1.6	0.5	3.1	33.2	13.0	-7.9	-5.0	-2.9
Commercial banks	(-2.8)	(-4.8)	(3.7)	(29.9)	(5.0)	(-5.9)	(-5.0)	(-2.9)
Nonbanks	(2.2)	(1.8)	(3.4)	(3.9)	(7.5)	(-2.0)	(--)	(--)
Residual	(-1.0)	(3.5)	(-4.0)	(-0.6)	(0.5)	(--)	(--)	(--)
	(In per cent of GDP)							
Total revenue	2.72	25.4	24.3	25.9	27.1	28.9	30.0	30.3
Of which: Government current revenue	(27.1)	(24.8)	(24.2)	(25.5)	(26.8)	(26.7)	(27.9)	(28.2)
Total expenditure	40.3	42.3	55.1	59.3	59.8	56.3	48.2	46.5
Of which: Government current expenditure	(26.6)	(25.7)	(24.7)	(23.2)	(24.2)	(25.3)	(25.4)	(24.6)
Capital expenditure	(13.6)	(16.7)	(30.1)	(36.1)	(35.7)	(31.0)	(22.7)	(21.9)
Current balance	0.4	-0.3	-0.7	2.7	2.9	3.5	4.6	5.7
Of which: Government	(0.5)	(-0.9)	(-0.4)	(2.3)	(2.6)	(1.4)	(2.4)	(3.6)
Overall balance	-13.1	-16.9	-30.7	-33.4	-32.7	-27.5	-18.2	-16.2
Overall balance after grants	-3.9	-2.1	-17.2	-17.9	-17.8	-14.9	-10.9	-8.5
Nonconcessional financing	0.7	0.6	9.5	12.9	11.5	7.0	0.5	0.8
External	(1.5)	(0.2)	(8.3)	(1.5)	(7.2)	(9.4)	(1.9)	(1.5)
Domestic	(-0.8)	(0.4)	(1.2)	(11.4)	(4.3)	(-2.4)	(-1.4)	(-0.7)
Of which: banks	/-1.4/	/-2.1/	/1.4/	/10.3/	/1.6/	/-1.8/	/-1.4/	/-0.7/

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

1/ Year beginning July 1.
2/ Of this, EC$11.8 million is from sources not yet identified.
3/ Of this, EC$0.4 million is from sources not yet identified.

growth in revenue, rising by 31.5 per cent annually from 1979 to 1982. Current outlays rose by only 8.5 per cent a year in this period, and the public sector current account shifted from a deficit equivalent to 2.3 per cent of GDP in 1978 to a surplus of 2.7 per cent of GDP in 1982.

Although all categories of investment have risen over the past four years, Grenada's public sector investment program (PSIP) has been dominated by a project to build a new international airport at Point Salines, near the capital. In the four-and-a-half years through mid-1983 outlays on this project amounted to EC$150 million (US$55.5 million) and represented 48 per cent of total public investment expenditure over the period. Two thirds of the cost of the airport in this period was covered by foreign grants and concessionary loans, mainly grants from Cuba which have covered almost half of the total project cost so far. Equipment for the project has been financed by suppliers' credits of EC$19 million from the United Kingdom and Finland. As of mid-1983 the airport was about 80 per cent completed; outlays of EC$41 million are required to finish it, and the airport is expected to become operational by mid-1984. Of the remaining outlays, half will be covered by already committed grants, and most of the rest by suppliers' credits that have already been contracted.

The airport project has been a priority of successive Governments of Grenada since the mid-1960s. The existing airport has a short runway, cannot accommodate international jet flights or night landings, and is located about 18 miles from the capital, linked by a winding mountain road. In 1976 a World Bank mission recommended evaluation of the feasibility of a new airport with a 5,000 foot runway at Point Salines. Following further engineering work and with the pledge of substantial assistance from Cuba, the new Government of Grenada in 1979 began construction of an airport with a 9,000 foot runway. At that time the World Bank took the position that no adequate feasibility study had been done, while the Government argued that a consideration of the opportunity costs of the various alternatives was not strictly relevant given the high grant element in the financing of the project.

In September 1982, the World Bank judged the sectorial composition of Grenada's public investment program other than the airport to be generally appropriate to the Government's development priorities, which focus on agriculture, forestry, fisheries, and tourism. However, it stated that it was not in a position to judge the economic or financial merits of the airport project nor the quality of other individual projects in the program. This assessment also holds for the investment program for the period covered by the proposed extended arrangement. The Bank is considering financing for a loan to the private agricultural sector in Grenada in the near future. The project is being prepared with the participation of FAO.

There are 28 nonfinancial public enterprises (NPE), a number of which have been set up in the past three years and some which have not yet started operations. According to detailed information on 11 major enterprises, which account for about three quarters of the total capital expenditure of the NPE, the current account of the NPE fluctuated around balance in 1978-81, and shifted to a surplus of 0.3 per cent of GDP in 1982--a level of surplus which is likely to be repeated in 1983. This improvement partly reflected increases in water rates in 1981 and 1982, an increase in telephone and electricity rates in 1982, and generation of an operating surplus by the Marketing and National Importing Board (MNIB).

The current account deficit of the balance of payments widened from the equivalent of 7 per cent of GDP (US$5.2 million) in 1979 to 33.2 per cent of GDP (US$35.7 million) in 1982 (Table 4). Besides mirroring the upsurge in public investment and associated imports, the weakening in the current account also reflected a 13 per cent drop in export earnings from 1979 to 1982 and a 15 per cent decline in tourist receipts. The fall in export earnings is explained by adverse price developments as export prices fell by 20 per cent from 1979 to 1982. Export volume of major crops was constrained by low international demand; stocks of nutmeg rose by 65 per cent to 7.8 million pounds in 1981-82, an amount which represents one and a half years of export shipments. Nontraditional exports expanded to a level of US$4.1 million in 1982, compared with US$0.7 million in 1979. Imports doubled over the period 1979-82, primarily because of the public investment program. The 28 per cent drop in stayover tourist arrivals from 1979 to 1982 was considerably greater than the 5 per cent drop in tourism in the region in the same period; the decline reflected not only the world recession, but also the effects of the closure of the 184-room Holiday Inn in 1981 as a result of fire damage. The Holiday Inn represents about one quarter of Grenada's international-class tourist capacity. In percentage terms, the decline in tourist arrivals was about the same over the period for the United States, Canada, the United Kingdom, and Germany. Over the past few years the current account deficits were covered mostly by inflows of external grants and concessionary loans, but also in part by borrowing from the Fund in 1981 and by inflows of commercial bank capital in 1982.

The expansion of nontraditional exports in the past few years largely resulted from new private investments, particularly in the garment industry. A modest revival in private investment appears to be under way. Applications for fiscal incentives approved in 1982 involved investments of EC$3.5 million, up from EC$1.4 million in the previous year, and in the first five months of 1983 applications were submitted involving a further EC$2.2 million. Loan applications and approvals by the Grenada Development Bank also rose in 1982, and there are currently four private sector loan applications at the Caribbean Development Bank for tourism projects with a combined value of EC$7.4 million. There was also some turnaround in exports and tourism in early 1983, when merchandise and tourist receipts were 18 and 8 per cent higher, respectively, than in the same period of 1982.

Table 4. Grenada: Balance of Payments

	1979	1980	1981	1982	Est. 1/ 1982/83	Projections 1/ 1983/84	1984/85	1985/86
	(In millions of U.S. dollars)							
Current account	-5.2	-13.3	-23.2	-35.7	-34.8	-33.2	-24.2	-25.2
Goods and services	-13.2	-26.1	-37.8	-50.1	-49.1	-47.7	-40.7	-42.7
Merchandise trade	-27.9	-40.1	-44.1	-52.7	-52.9	-54.5	-55.0	-62.7
Exports, f.o.b.	(21.4)	(17.4)	(19.0)	(18.6)	(19.5)	(22.1)	(24.5)	(28.9)
Imports, c.i.f.	(-49.3)	(-57.5)	(-63.1)	(-71.3)	(-72.4)	(-76.6)	(-79.5)	(-91.6)
Of which: airport related	/2.4/	/4.7/	/6.2/	/8.8/	/12.9/	/9.6/	/0.2/	/--/
Services	14.7	13.4	6.3	2.6	3.8	6.8	14.3	20.0
Travel receipts	(15.3)	(16.5)	(13.9)	(13.0)	(13.7)	(16.1)	(21.1)	(27.0)
Travel payments	(-3.3)	(-3.2)	(-3.9)	(-3.3)	(-3.4)	(-4.0)	(-4.2)	(-5.6)
Interest of public debt	(-0.4)	(-0.4)	(-0.6)	(-0.8)	(-1.4)	(-2.5)	(-3.5)	(-4.3)
ECCA profits	(0.5)	(0.7)	(0.8)	(1.1)	(1.1)	(1.1)	(1.2)	(1.3)
Other services (net)	(2.6)	(-0.2)	(-3.9)	(-7.4)	(-6.2)	(-3.9)	(0.2)	(1.2)
Private transfers (net) 2/	8.0	13.4	14.6	14.4	14.3	14.5	16.5	17.5
Capital account	6.2	13.7	18.1	33.8	35.3	28.6	21.6	22.9
Public sector grants	6.9	12.7	12.9	16.7	16.9	15.6	9.9	11.8
Public sector borrowing (net)	2.4	1.3	7.9	7.1	15.3	16.0	14.2	11.7
Commercial banks (net)	-1.1	1.1	-0.8	9.4	3.3	-2.2	-2.4	-1.3
Private investment	--	--	--	1.9	1.4	1.0	1.9	3.1
Currency holdings 3/	-2.0	-1.4	-1.4	-1.3	-1.6	-1.8	-2.0	-2.4
Errors and omissions	-2.6	-0.8	-2.9	2.0	-1.2	--	--	--
SDR allocations 4/	0.8	0.5	0.4	--	--	--	--	--
Overall surplus or deficit (-)	-0.8	0.1	-7.6	0.1	-0.7	-4.6	-2.6	-2.3
Financing	0.8	-0.1	7.6	-0.1	0.7	4.6	2.6	2.3
IMF (net)	0.5	--	6.0	-0.9	-0.8	4.6	2.6	2.3
ECCA borrowing	0.4	0.3	0.8	0.8	0.7	--	--	--
Government foreign assets	-0.1	-0.4	1.0	--	0.8	--	--	--
	(In per cent of GDP)							
Current balance	-6.9	-15.5	-24.2	-33.2	-30.7	-26.7	-17.7	-16.5
Excluding airport	(-3.7)	(-10.0)	(-17.7)	(-25.0)	(-19.3)	(-17.7)	(-17.6)	(-16.5)
Overall balance	-2.0	-1.1	-7.9	0.1	-0.6	-3.7	-1.9	-1.5
Memorandum items								
Banana exports ('000 tons)	14.1	12.5	10.2	9.8	10.3	10.6	11.1	12.3
Cocoa exports ('000 tons)	2.4	1.9	2.7	2.1	2.4	2.5	2.7	2.9
Nutmeg exports ('000 tons)	2.3	1.5	1.7	2.1	2.7	2.5	2.6	2.8
Stayover visitors ('000)	32.3	29.4	25.1	23.2	24.2	26.5	30.9	36.3
Debt service ratio 5/	3.7	3.0	2.7	4.5	4.6	7.7	12.2	12.6

Sources: Ministry of Planning, Finance and Trade; Statistical Office; and Fund staff estimates.

1/ Refers to year beginning July.
2/ Includes migrant transfers, workers' remittances, other transfers from Grenadians living abroad, and medical students transfers for expenses not covered by payments made abroad to the school.
3/ East Caribbean dollars in circulation.
4/ Includes profits from gold sales.
5/ Interest and amortization as per cent of receipts from exports, services, and private transfers.

Grenada's external debt (including debt owed to the Fund) rose from US$10.3 million (16 per cent of GDP) in 1978 to US$30.8 million (28.7 per cent of GDP) in 1982, and is projected to reach US$52.4 million (44 per cent of GDP) by the end of 1983. As most of the external loans are on concessional terms, debt service in relation to exports of goods, services, and private transfers has remained low, rising from 2.6 per cent in 1978 to 4.5 per cent in 1982; the debt service ratio is expected to remain unchanged in 1983.

The local commercial banks were able to improve their net foreign asset position 1/ slightly during 1978-81, as domestic credit expansion was smaller than the growth of deposits; in this period, outstanding credit to the public sector declined, while credit to the private sector (including commodity boards) expanded at a rate of about 12 per cent a year. However, in 1982 and early 1983, the commercial banks have faced a severe liquidity squeeze following an EC$30 million rise in public sector net borrowing that was affected in part through the doubling of the special deposit requirement. As a result, the ratio of net foreign assets to total deposits fell from 24 per cent at the end of 1981 to 4 per cent at the end of 1982 (in the government-owned National Commercial Bank the ratio fell from 39 per cent to 2 per cent during the same period). This liquidity squeeze led to the imposition of severe restraints on new lending by the two private banks in operation (the third bank, the Royal Bank of Canada, sold its operations to the Government in January 1983).

Market interest rates tended to move upward in 1982 and early 1983. Commercial banks raised the maximum deposit rate from 5-1/2 per cent that had prevailed since the beginning of 1979 to 7 per cent in March 1983 and to 9 per cent on large deposits in April 1983. Lending rates, which were around 9 per cent during most of the 1979-81 period, moved close to the statutory limit of 12-1/2 per cent in the latter half of 1982 and early 1983. These rates are slightly lower than rates in other ECCA countries, and, as in the other ECCA countries, tended to be lower than the domestic rate of inflation and deposit rates in major international financial centers in the early 1980s.

III. The EFF Program

The three-year program of the Grenadian authorities has as its principal objective a reduction in the financial imbalances in the economy, a strengthening of the balance of payments position, a buildup in the country's net foreign assets, and completion of the core investments necessary for generating sustainable growth. The public finances are a major focus of the program, with the aim of securing a reduction in the overall deficit, especially in the use of nonconcessionary financing, and a further improvement in the savings effort. To this end, the

1/ The banks' liquid assets and net foreign assets are virtually synonymous because of the absence of a local money market.

fiscal program involves an improved revenue effort, restraint in public sector wages and employment, and restraint in other expenditure policies. Tighter fiscal management, together with a recovery in exports and tourism, is expected to lead to a reduction in the current account deficit in the balance of payments during the program period, and to a stabilization of the debt service ratio.

a. Growth and balance of payments

Grenada's medium-term prospects depend heavily on the extent of the response of the private sector, both domestic and foreign, to the new infrastructure that is being put in place. Grenadian officials believe that the response in tourism and agricultural exports will be very substantial because, in their view, inadequate economic infrastructure (and particularly inadequate air access) has been an important constraint on economic growth and on private sector activity. The mission also stressed the importance of providing an appropriate "climate" for the private sector.

The Government believes that investment in new infrastructure, wage restraint, improved labor relations and the implementation of a three-year financial program supported by the Fund will provide a favorable environment for private investment, particularly in tourism and in manufacturing. A new investment code published in April 1983 provides guarantees and fiscal incentives for local and foreign private investment similar to those given by other countries in the region. The code makes it clear that it is the policy of the Government to avoid compulsory acquisition of enterprises, but that if this becomes necessary it will be carried out on the basis of adequate compensation under existing laws, and at a price to be agreed through negotiation.

The Government has plans to expand the role of the state trading corporation (MNIB) over the next few years, and wants to encourage local private traders to move into tourism and manufacturing. The Government seeks to use MNIB to obtain favorable import prices and to provide stability to domestic prices through bulk purchases from traditional and nontraditional sources. At present the MNIB imports rice, sugar, powdered milk, cement, and some fertilizers and tires. In its discussions with the authorities, the mission pointed to the apprehensions of the local private sector about the future role of the MNIB in the economy. Subsequently, the Government announced that over the next three years the MNIB will not be granted any import monopolies but that it will be able to import any product in competition with private importers under the same conditions as the private sector regarding the granting of import licenses, and payment of import duties and taxes (see paragraph 7 of the letter of intent). This policy is expected to help strengthen business confidence.

Over the medium term, the Grenadian authorities foresaw a very rapid upturn in tourism, and expected real growth to be in the range of 5 to 7 per cent a year. In assessing the medium-term outlook the mission took a more cautious view than the authorities, forecasting growth of real GDP of 2.3 per cent in the first year, rising to 3 per cent and 5 per cent in the subsequent program years. Export receipts are projected to rise by 13, 11, and 18 per cent, respectively, in the three years of the program. Stayover tourists are expected to recover close to the 1979 levels by the second year of the program and to increase to 12 per cent above the 1979 levels in the third year.1/ The current account deficit in the balance of payments is expected to drop to about 16-1/2 per cent of GDP in 1985/86 from almost 31 per cent of GDP in 1982/83. Balance of payments projections are shown in Table 4.

With the expiration of grace periods on borrowings already undertaken and disbursement of already contracted commercial loans, debt service will rise rapidly during the program period, although it should still be within manageable limits (Table 5). In relation to receipts from exports of goods, services, and private transfers, debt service is expected to rise from 4-1/2 per cent in 1982/83 to a peak of about 12-1/2 per cent in 1985/86, and drop back thereafter.

Projections of tourism for the program period and beyond are particularly problematical. The increase in tourist arrivals projected for the program period can be accommodated with the existing stock of hotel rooms, provided the Holiday Inn is put back into full operation within the next two years. The assets were recently purchased by the Government, and the rooms (none of which were damaged by the 1981 fire) will be put back in operation by August 1983. Various alternatives for the hotel are being explored with the help of IFC and the CDB, including possible private participation. A number of other private sector hotel projects, both local and foreign, are at various stages of preparation, but it is unclear how soon they will be implemented. At the same time several airlines are indicating the possibility of providing air service to Grenada once the new airport is open, but few arrangements have been firmed up as yet.

Besides tourism, the Government is also placing heavy emphasis on agriculture. The public sector investment program includes feeder roads, crop rehabilitation and diversification, and fisheries projects, and, as noted above, the World Bank is considering a loan to the private agricultural sector in the near future. The Government's plans in agriculture rely heavily on improving the efficiency of the Grenada Farms Corporation (GFC), which operates 4,000 acres in some 30 farms. Most of these estates were acquired by previous governments, though recently there has been a further increase in acreage through purchase or lease under the Land Utilization Act which provides a procedure for compulsory acquisition or leasing at market value of idle land. The GFC has been reorganized into seven regional units headed by qualified managers, and the corporation is upgrading its operations.

1/ The projection for 1985/86 is 8 per cent higher than that of the latest (1982) World Bank Economic Memorandum on Grenada (3825-GRD).

Table 5. Grenada: Projections of Debt Service on Government and Government-Guaranteed External Debt

	July-June						
	1982/83	1983/84	1984/85	1985/86	1986/87	1987/88	1988/89
	(In thousands of U.S. dollars)						
Total debt service 1/	2,601	4,852	8,941	10,792	10,865	12,138	14,138
Interest	1,386	2,503	3,515	4,285	4,846	4,916	4,608
Principal	1,215	2,349	5,426	6,507	6,020	7,222	9,530
Total debt service excluding IMF	1,676	3,586	6,031	7,423	8,149	9,393	10,645
On debt contracted by June 30, 1983	1,669	3,490	5,642	6,548	6,740	7,330	7,466
On additional concessional debt	7	96	389	875	1,409	2,063	3,179
IMF debt service 1/	925	1,266	2,910	3,369	2,716	2,745	3,493
Charges	428	574	910	1,194	1,328	1,270	1,113
Repurchases	497	692	2,000	2,176	1,388	1,475	2,380
Memorandum items							
Outstanding external debt							
Excluding IMF	35,280	51,300	65,500	77,200	89,700	96,900	100,700
Including IMF 1/	42,080	62,680	79,440	93,480	105,040	110,800	112,300
Receipts from exports, services, and private transfers	56,200	63,000	73,200	85,900	94,700	104,800	115,400
	(In per cent)						
Debt service excluding IMF/receipts from exports service, and private transfers	3.0	5.7	8.2	8.6	8.6	9.0	9.2
Total debt service/receipts from exports, services, and private transfers	4.6	7.7	12.2	12.6	11.5	11.6	12.3
Average interest rate	4.0	4.8	4.9	5.0	4.9	4.6	4.6
Outstanding debt (including IMF)/GDP	37.1	50.5	58.2	61.0	61.2	57.7	52.2

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

1/ Includes trust fund operations.

b. Fiscal policies

(i) The fiscal deficit and its financing

Under the program, the overall deficit, before official grants and concessionary loans, will decline to 16.2 per cent of GDP in 1985/86, from an estimated 32.7 per cent of GDP in 1982/83. After grants, the overall deficit is programed to decline to 8.5 per cent in 1985/86, from 17.8 per cent of GDP in 1982/83, and the use of nonconcessionary financing (a major focus of the program) is to decline from 11.5 per cent of GDP in 1982/83 to less than 1 per cent a year in 1984/85 and 1985/86. Any borrowing from ECCA during the program period is to be held in reserve in the government-owned commercial banks. In light of the growing debt service burden, no new borrowing or guaranteeing of loans on commercial terms, other than loans already contracted before the program period and the use of Fund resources, is to be undertaken, unless there is agreement with the Fund. Such agreement would be envisaged only in the event that a government-guarantee is required to facilitate a major private investment. It is to be noted that the authorities would like the Fund to give favorable consideration to higher use of Fund resources during the program period, and to the utilization of any SDR allocation during the program period.

(ii) Revenue and expenditure policies

New revenue measures designed to yield EC$4.2 million (1.3 per cent of GDP) were introduced in June, and may also be required in the second and third years, as current expenditure, despite a tight wage policy, is expected to rise slightly in relation to GDP during the three-year period, mainly because of the operating costs of the new airport and rising interest payments. The annual increase in the central government wage bill is to be held to 5-1/2 per cent a year for January 1984, which is 1-1/2 per cent below the projected rate of inflation (see paragraph 11 of the letter of intent). The wage bill covers wage rates, merit increases and changes in employment of both established and other government workers, including casual labor. The present three-year wage contract with the civil servants expires at the end of 1983. Salary increases in the rest of the public sector also will be restrained so that the projected operating surpluses can be realized. Thus, the program aims at raising public sector savings over the three-year period by the equivalent of close to 3 per cent of GDP (from 2.9 per cent to 5.7 per cent of GDP).

The revenue performance in the program period is helped by the new National Insurance Scheme, which is expected to generate significant surpluses. In the rest of the public sector, government policy is that social services (such as the National Transport Service) should cover their operating costs, and that other entities (including public utilities) should generate operating surpluses to cover a portion of their investments. Utility rates will be adjusted as necessary to provide an adequate rate of return on capital, in line with the guidelines of the CDB.

(iii) Public investment

In the context of the discussions on an EFF program, a detailed restructuring of the planned public sector investment program (PSIP) was undertaken by the Government of Grenada with the aim of reducing the use of local funds and recourse to nonconcessional financing as far as possible. The revised three-year PSIP amounts to EC$278 million (about 24 per cent of GDP a year). The program is still heavily concentrated on economic infrastructure; outlays to finish the international airport amount to almost 40 per cent of the PSIP in the first year and about 15 per cent of total over the three-year period (Table 6). Other significant infrastructure outlays involve the port, electricity, telephones, water and roads, which are seen as an integrated package of infrastructural requirements and as a prerequisite for the expected expansion of private investment in the hotel sector. The agricultural sector is slated to receive one fourth of total public sector investment outlays over the period, with cocoa and banana rehabilitation programs and fisheries development figuring prominently.

The three-year PSIP is expected to be financed from external grants (EC$101 million), concessionary external loans (EC$123 million), already contracted nonconcessionary external loans (EC$17 million), and budget resources (EC$38 million). About 25 per cent of the concessionary loans and 45 per cent of the grants are being provided by centrally planned economies, with Cuba and the German Democratic Republic the principal sources. The Caribbean Development Bank (CDB) is another major source of financing, with programed outlays of EC$85 million over the three-year period. With the exception of EC$12 million, all of the expected foreign grants and loans have been pledged. The program includes a contingency of EC$1 million in the first year, rising to EC$3.3 million in the third year, for unforeseen local currency expenditures.

Grenada has raised the level of investment dramatically over the past four years with the help of a substantial inflow of skilled and unskilled expatriates and returning citizens. The expatriate manpower involved in the airport project is expected to remain in the country after the completion of the project to support the country's absorptive capacity during the remainder of the program period.

c. Money and credit

The monetary program aims at rebuilding the liquidity of the banking system while at the same time ensuring adequate financing for the private sector. The program incorporates a plan to rebuild the foreign assets of the government-owned commercial banks to 10 per cent of their deposit liabilities by the end of the first year of the program, 18 per cent by the end of the second year, and 20 per cent by the end of the third year (Table 7). This is to be achieved mainly through a reduction in outstanding public sector net borrowing from these banks. Public sector net borrowing from the private banks would remain unchanged

Table 6. Grenada: Public Sector Investment Program

(In millions of East Caribbean dollars)

	Est. 1/	Program 1/		
	1982/83	1983/84	1984/85	1985/86
Total	109.0	103.9	83.8	90.4
Of which:				
International airport	64.6	40.0	1.0	--
Port expansion	2.0	3.9	1.2	--
Electricity expansion	0.5	3.9	1.3	0.7
Telephone expansion	4.5	3.7	2.6	--
Water systems	0.9	2.5	3.4	7.9
Roads	5.1	7.6	14.8	14.8
Agriculture	13.5	20.2	23.0	24.4
Industry	0.4	3.4	9.9	10.0
Other (incl. contingency)	14.9	18.7	28.6	32.6
Financing				
Grants	45.5	42.1	26.8	31.8 2/
Concessional loans (gross)	21.3	32.1	47.6 3/	43.4 3/
Nonconcessional loans (gross)	21.9	16.8	--	--
General budgetary resources	20.3	12.9	9.4	15.2

Sources: Ministry of Planning, Finance and Trade; and Inter-Agency Resident Mission, Antigua.

1/ Year beginning July 1.
2/ Of this, EC$11.8 million is from sources not yet identified.
3/ Of this, EC$0.4 million is from sources not yet identified.

Table 7. Grenada: Monetary Projections for the First Program Year

	1983											
	March			June (Est.)			September			December		
	All Banks	Govt. Banks	Other Banks	All Banks	Govt. Banks	Other Banks	All Banks	Govt. Banks	Other Banks	All Banks	Govt. Banks	Other Banks
	(In millions of East Caribbean dollars)											
Net foreign position	3.5	-0.5	4.0	5.0	1.5	3.5	6.6	2.5	4.1	8.6	3.9	4.7
Net domestic credit	121.8	59.8	62.0	121.9	59.5	62.4	123.8	60.3	63.5	125.4	60.7	64.7
Central Government (net)	42.8	23.0	19.8	44.4	24.5	19.9	44.3	24.4	19.9	42.5	22.6	19.9
Nonfinancial public enterprises	7.2	3.5	3.7	7.6	3.9	3.7	7.7	4.0	3.7	7.8	4.1	3.7
Private sector	84.9	39.4	45.5	83.0	37.9	45.1	84.9	38.7	46.2	88.2	40.8	47.4
Other (net)	-13.1	-6.1	-7.0	-13.1	-6.8	-6.3	-13.1	-6.8	-6.3	-13.1	-6.8	-6.3
Deposit liabilities	125.3	59.3	66.0	126.9	61.0	65.9	130.4	62.8	67.6	134.0	64.6	69.4
Nonfinancial public enterprises	2.7	2.0	0.7	3.7	3.0	0.7	3.8	3.1	0.7	3.9	3.2	0.7
Private sector	98.2	47.3	50.9	101.4	50.7	50.7	104.4	52.2	52.2	107.5	53.7	53.8
Nonresident	24.4	10.0	14.4	21.8	7.3	14.5	22.2	7.5	14.7	22.6	7.7	14.9
	(In per cent)											
Net foreign position/ deposit liabilities	2.8	-0.8	6.1	3.9	2.5	5.3	5.1	4.0	6.0	6.4	6.0	6.8

	1984											
	March			June			June 1985			June 1986		
	All Banks	Govt. Banks	Other Banks	All Banks	Govt. Banks	Other Banks	All Banks	Govt. Banks	Other Banks	All Banks	Govt. Banks	Other Banks
	(In millions of East Caribbean dollars)											
Net foreign position	10.5	5.3	5.2	12.4	6.7	5.7	20.3	13.3	7.0	25.5	16.8	8.7
Net domestic credit	125.7	60.4	65.3	126.1	60.1	66.0	131.7	60.5	71.2	145.0	67.0	78.0
Central Government (net)	41.4	21.5	19.9	38.5	18.6	19.9	33.4	13.6	19.8	30.5	10.7	19.8
Nonfinancial public enterprises	7.9	4.2	3.7	7.9	4.2	3.7	8.9	5.2	3.7	10.9	7.2	3.7
Private sector	89.5	41.5	48.0	92.8	44.1	48.7	102.5	48.5	54.0	116.7	55.9	60.8
Other (net)	-13.1	-6.8	-6.3	-13.1	-6.8	-6.3	-13.1	-6.8	-6.3	-13.1	-6.8	-6.3
Deposit liabilities	136.2	65.7	70.5	138.5	66.8	71.7	152.0	73.8	78.2	170.5	83.8	86.7
Nonfinancial public enterprises	4.0	3.3	0.7	4.0	3.3	0.7	5.0	4.3	0.7	7.0	6.3	0.7
Private sector	109.2	54.6	54.6	111.1	55.5	55.6	122.1	61.0	61.1	137.0	68.5	68.5
Nonresident	23.0	7.8	15.2	23.4	8.0	15.4	24.9	8.5	16.4	26.5	9.0	17.5
	(In per cent)											
Net foreign position/ deposit liabilities	7.7	8.0	7.4	9.0	10.0	8.0	13.4	18.0	9.0	15.0	20.0	10.0

Source: Fund staff estimates.

1/ Data for June 1983, the base period for the projections, are estimated on the basis of balance sheet data for March 1983 and partial information for the period April-June 1983.

during the period; in line with this policy, the 20 per cent special deposit requirement will be reduced in quarterly steps to 16 per cent by the end of the first program year and further in subsequent years. Coupled with the expected normal growth in deposits, these measures are expected to be sufficient to ensure an increase of about 12 per cent a year in bank credit to the private sector over the program period. The authorities plan to utilize selective credit controls and limits on consumer credit in order to try to channel credit into productive investment.

Given Grenada's institutional framework, there is little scope for monetary or exchange rate policy. Not only has Grenada no central bank of its own, but ECCA has used its somewhat limited statutory powers only sparingly. Agreement was reached recently among the member states on transforming ECCA into a central bank by October 1983.

The government-owned banks have been encouraged to compete actively for deposits. A ceiling of 12-1/2 per cent on lending rates has been in existence for a number of years. In May 1981 the Government issued a decree raising the ceiling to 17-1/2 per cent, but in view of strong opposition from the banks and the private sector, and of the fact that the new ceiling was out of line with those in other ECCA countries, the decree was rescinded two weeks later. With the slowdown in domestic inflation and declining rates abroad, the interest rate structure, at least on large deposits, is now positive in real terms and not significantly out of line with those abroad. However, the real average deposit rate is still slightly negative, and the authorities expect to review the interest rate policy in Grenada in the context of a coordinated regional interest rate strategy to be developed by the regional central bank.

d. Exchange and trade system

With minor exceptions, the trade system of Grenada is free of restrictions. Grenada is a member of CARICOM and a signatory of its various protocols. A tax of 2-1/2 per cent was imposed on foreign exchange purchases for budgetary purposes in April 1977 and was doubled in March 1978. The Fund has approved the multiple currency practice that arises from this tax on various occasions, most recently until September 30, 1983, or the conclusion of the Article IV consultation, whichever came first. The Grenadian authorities are not inclined to reduce this tax until alternative revenue sources can be identified, and are requesting technical assistance from the Fund for the latter purpose (paragraph 13 of the letter of intent). Payments and transfers for current international transactions are monitored but not restricted, except for the above-mentioned tax on purchases of foreign exchange. The surrender of exchange proceeds from exports and invisibles is mandatory, but is not enforced. Although transfers of capital outside the ECCA area are in principle restricted, these restrictions cannot be effective as there is broad freedom of capital movements within the ECCA region, and exchange controls vis-a-vis the rest of the world differ in scope and degree of enforcement among ECCA's member states.

The exchange rate of Grenada's currency, the East Caribbean dollar, can only be changed by agreement of all the members of ECCA. The East Caribbean dollar has been pegged to the U.S. dollar at EC$2.70 per U.S. dollar since July 1976. From the end of 1980 to March 1983 the trade-weighted exchange rate for the Grenada East Caribbean dollar has appreciated by some 28 per cent in nominal terms and by about 30 per cent in real effective terms (Chart 1). The Grenadian authorities were aware that the appreciation of the East Caribbean dollar had been somewhat larger for them than for other ECCA countries because of the bigger share of countries other than the United States in Grenada's trade and tourism. They said that they would review the regional exchange rate level and system with other members of the Eastern Caribbean Central Bank, but it was uncertain whether agreement would be reached on any modification of the parity. The staff stressed the implications of the current exchange rate for adjustment policies, particularly the need for measures to offset the adverse effect on government revenue and the need for wage restraint to contain costs.

e. Performance criteria and consultation clause

Performance criteria (Table 8) are (1) quarterly ceilings on the nonconcessional sources of financing of the overall public sector (defined as Central Government, National Insurance Scheme, and all state enterprises); the use of foreign grants and concessionary loans will not affect the ceiling; (2) quarterly floors on the net foreign asset positions of the two government-owned commercial banks; (3) a prohibition on contracting of public or publicly guaranteed foreign debt at nonconcessional terms; (4) an undertaking to reach understandings with the Fund for subsequent years of the arrangement before the beginning of the second and third years, respectively; (5) a mid-term review clause prior to the 1984 budget; and (6) the normal injunctions relating to exchange and trade restrictions.

IV. Staff Appraisal

The Government of Grenada has been undertaking an ambitious investment program in order to raise the country's growth potential. The centerpiece of this program has been a US$70 million international airport, which is expected to give a boost to tourism and nontraditional exports. About 80 per cent of planned expenditure on the airport has already taken place, with large-scale grants and loans from various countries.

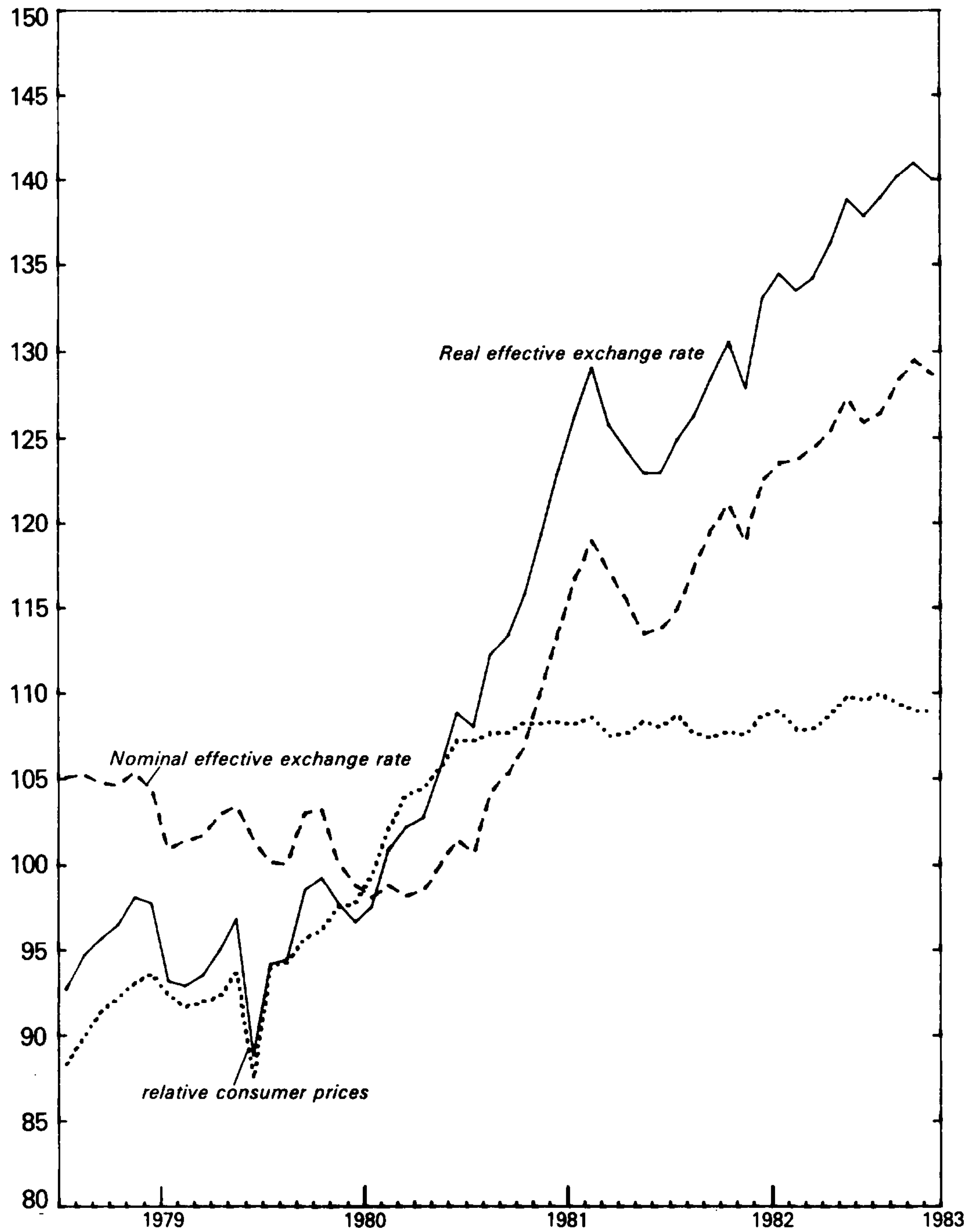
Grenada's recent economic performance has been hampered by the world recession. Nonetheless, real GDP grew by an average of 3 per cent a year in 1980-82, led by construction. The rate of inflation has dropped to about 5-1/2 per cent from an average of 20 per cent a year in 1980-81. Grenada's current account deficit in the balance of payments widened to US$36 million in 1982, or 33 per cent of GDP, from 7 per cent of GDP in 1979, due to adverse movements in the

CHART 1

GRENADA

EFFECTIVE EXCHANGE RATE INDICES, 1979-83[1]

(1980 = 100)



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

[1]The indices are weighted with the trade and tourist shares of Grenada's major trading partners. An increase in the indices reflects an appreciation of the East Caribbean dollar.

Table 8. Grenada: Quantitative Performance Criteria Through June 1984

	1983				1984	
	Actual Mar. 31	Est. June 30	Sept. 30	Dec. 31	March 31	June 30
	(In millions of East Caribbean dollars)					
Public sector nonconcessional borrowing (cumulative change) 1/			6.8	14.6	19.5	23.6
Net foreign assets of state banks 2/	-0.5	1.5	2.5	3.9	5.3	6.7

1/ Nonconcessional external loans (as defined by the World Bank but excluding loans from CDB and OPEC), changes in government sinking fund balances, net borrowing from IMF, SDR allocations, net borrowing from ECCA, and net borrowing from local commercial banks, nonbanks, insurance companies and other domestic sources. The limits include provision for EC$16.8 million of nonconcessional foreign borrowing disbursed in equal quarterly installments; the quarterly limits will be adjustable in the event of deviations from the expected disbursement schedule for these specific loans.

2/ Includes cash, balances due from ECCA, balances due from ECCA area banks other than in territory, and balances due from banks abroad less borrowing and balances due to ECCA, balances due to ECCA area banks other than in territory, and balances due to banks abroad, of the National Commercial Bank and the Grenada Bank of Commerce. In the event that the Government of Grenada borrows (net) from the East Caribbean Currency Authority, then ceilings will be adjusted upward by the corresponding amount.

terms of trade, a decline in tourist arrivals, and a sharp rise in imports related to investment spending. These growing deficits have been financed mostly by foreign aid inflows, but also by borrowing from the Fund and, more recently, by inflows of commercial bank capital. Though external debt has risen quite rapidly in recent years, most of it has been on concessional terms, and the debt service ratio (4-1/2 per cent) is still quite low.

Despite a recent improvement in the public sector savings performance, the public finances have shown large and growing overall deficits as a result of the steep rise in investment spending; the deficit reached the equivalent of 33 per cent of GDP in 1982. Although foreign aid flows continue to cover the bulk of the deficits, there has been substantial recourse to other financing in the last two years, particularly in 1982 when heavy borrowing from the domestic banking system resulted in a steep drop in the banks' liquid asset holdings.

The program recommended to be supported by the proposed EFF arrangement has as its main objectives a reduction in the financial imbalances in the economy, a strengthening of balance of payments position, and a buildup of government foreign reserves, while at the same time completing investments necessary for generating sustainable growth. The principal fiscal targets include a reduction in the overall deficit to about 16 per cent of GDP from almost 33 per cent in the twelve months through June 1983, an increase in public sector savings of almost 3 per cent of GDP over the three-year period, and a reduction in the use of nonconcessionary finance to less than 1 per cent of GDP a year in the final two program years. Apart from loans already contracted and borrowing from the Fund, there is to be no further foreign borrowing at nonconcessional terms during the program period. The program includes a plan to rebuild the net foreign assets of the two government-owned commercial banks to 20 per cent of their liabilities by the third year of the program. This is needed to reinforce their domestic and international creditworthiness.

Given the island's resources, the Government's emphasis on agriculture and tourism is fully appropriate. This view is shared by the World Bank which has noted that since both agriculture and tourism have a good employment potential, the goal of increasing exports should be compatible with the goal of increasing employment. The staff recognizes the need to remove the deficiencies of infrastructure that constrained output growth in the past, but large-scale involvement of the private sector (both domestic and foreign) will be required if the opportunities created by the new infrastructure are to be exploited. The staff, therefore, welcomes the recent moves to encourage the private sector, including the new Investment Code and the clarification of the future role of the Marketing and National Importing Board. It will be important to work further to build up the confidence of the private sector, and to improve Grenada's attraction in traditional tourist markets if the Government's development goals are to be realized.

The required adjustment of the public finances will depend heavily on the adoption of a restrictive wage policy. Because of the rising interest burden and the operating costs of the new airport, it is essential to restrain the growth of current outlays if a further increase in the already high tax burden is to be avoided. Wage restraint is also critical to the assurance of Grenada's international competitiveness, which has been adversely affected by the steep appreciation of Grenada's trade-weighted East Caribbean dollar over the past two years. In this connection, the staff would urge Grenada to review with the other ECCA members exchange rate policy for the East Caribbean dollar. Although domestic interest rates are much less out of line with domestic inflation and with rates abroad than they were a year ago, the authorities are encouraged to review the interest rate policy in the regional context with a view to promoting savings and better credit allocation.

In view of the Government's undertaking with regard to the reform of the tax system, the staff supports Grenada's request for approval of the temporary retention by Grenada of the multiple currency practice resulting from the 5 per cent tax on foreign exchange purchases until July 31, 1984, or the completion of the next Article IV consultation, whichever is earlier.

V. Proposed Decisions

(i) 1983 Consultation

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

1. The Fund takes this decision relating to Grenada's exchange measures subject to Article VIII, Section 3, and in concluding the 1983 Article XIV consultation with Grenada, in the light of the 1983 Article IV consultation with Grenada conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. Grenada applies a tax of 5 per cent on most purchases of foreign exchange, which gives rise to a multiple currency practice. In view of the circumstances of Grenada, the Fund approves the retention by Grenada of the multiple practice resulting from the tax on foreign exchange purchases until July 31, 1984, or the completion of the next Article IV consultation, whichever is earlier.

(ii) Extended Arrangement

1. The Government of Grenada has requested an extended arrangement for a period of three years from   , 1983 in an amount equivalent to SDR 13.5 million.

2. The Fund approves the extended arrangement attached to EBS/83/164 (8/8/83).

3. The Fund waives the limitation in Article V, Section 3(b)(iii).

Fund Relations with Grenada
(On June 30, 1983)

Membership date: August 27, 1975.

Status: Article XIV.

Quota: SDR 4.5 million.

Fund holdings of Grenada currency:

	Millions of SDRs	Per Cent of Quota
Total	8.80	195.59
Compensatory financing facility	(1.40)	(31.11)
Credit tranches	(2.90)	(64.44)

SDR Department:

	Millions of SDRs	Per Cent of Net Cumulative Allocation
Net cumulative allocation	0.93	100.00
Holdings	0.02	1.76

Trust Fund Loan outstanding: SDR 1.93 million.

Direct distribution of profits of gold sales: US$0.33 million.

Gold distribution (four distributions): 1,711.539 fine ounces.

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

Recent contacts: The last Article IV consultation discussions were held in November 1980. The consultation was concluded by the Executive Board on May 11, 1981. Missions visited Grenada in November 1981 and in May 1982. A staff member visited Grenada in March 1983 to update information. Mr. Stephens, the Fund's Regional Advisor in the East Caribbean, is accredited to Grenada.

Grenada--Basic Data

Area and population	
Area	133 sq. miles (344 sq. kilometers)
Population (end-1982)	111 thousand
Annual rate of population increase (1977-82)	0.9 per cent
GDP (1982)	SDR 97.5 million US$107.6 million EC$290.5 million
GDP per capita (1982)	SDR 790

	1979	1980	1981	Prel. 1982
Origin of GDP		(per cent)		
Agriculture, fisheries, and forestry	31	28	28	25
Manufacturing	3	3	3	3
Construction	2	4	6	7
Wholesale and retail trade	15	14	14	14
Transport and communications	6	6	6	6
Hotels and restaurants	3	3	2	2
Government and other services	38	40	39	41
Utilities	2	2	2	2
Ratios to GDP				
Exports of goods and nonfactor services	53.8	43.8	40.1	35.6
Imports of goods and nonfactor services	71.7	72.2	73.3	76.5
Current account of the balance of payments	-6.9	-15.5	-24.2	-33.2
Central government revenues	27.2	24.8	24.3	25.5
Central government expenditures	39.7	41.8	53.6	58.0
Central government savings	0.5	-0.9	-0.4	2.3
Central government overall surplus or deficit (-)	-12.5	-17.0	-29.2	-32.5
External public debt (end of year)	17.5	15.7	26.5	28.7
Gross domestic savings	-2.1	-6.2	0.3	-2.6
Gross investment	15.8	22.2	33.5	38.3
Money and quasi-money (end of year)	72.5	67.9	65.0	61.6
Annual changes in selected economic indicators				
Real GDP per capita	1.2	2.1	2.5	2.3
Real GDP	2.1	3.0	3.4	3.3
GDP at current prices	17.6	14.6	11.5	12.2
Domestic expenditure (at current prices)	24.0	24.8	15.7	18.7
Investment	(122.2)	(61.3)	(68.2)	(28.2)
Consumption	(16.0)	(19.2)	(4.7)	(15.5)
GDP deflator	14.8	14.4	9.6	7.5
Consumer prices (annual averages)	20.0	21.2	18.8	7.8
Central government revenues	23.0	4.7	9.2	17.8
Central government expenditures	41.1	20.8	42.7	21.6
Money and quasi-money	5.3	7.4	6.8	6.4
Money	(8.3)	(13.4)	(-1.9)	(6.2)
Quasi-money	(3.3)	(3.2)	(13.4)	(6.5)
Net commercial bank assets 1/	3.2	5.3	2.3	24.5
Credit to public sector (net)	(-3.8)	(-3.8)	(3.0)	(22.9)
Credit to private sector	(9.1)	(10.4)	(2.4)	(5.3)
Merchandise exports (f.o.b., in U.S. dollars)	26.6	-18.7	9.2	-2.1
Merchandise imports (c.i.f., in U.S. dollars)	38.1	16.6	9.7	13.6
Travel receipts (gross, in U.S. dollars)	6.2	7.8	-15.8	-6.5

Central government finances	1979	1980	1981	Prel. 1982
	(millions of East Caribbean dollars)			
Current revenue	54.9	57.5	62.7	74.2
Current expenditure	53.9	59.6	63.8	67.5
Current balance	1.0	-2.1	-1.1	6.7
Capital receipts	0.2	0.2	0.3	--
Capital expenditures	26.5	37.5	74.8	101.0
Overall balance	-25.3	-39.4	-75.6	-94.3
External grants and concessionary loans	24.6	37.9	54.8	59.7
Overall balance after grants and concessionary loans	-0.7	-1.5	-20.8	-34.6
External financing (net)	3.1	0.9	21.6	4.2
Internal financing (net)	-2.4	0.6	-0.8	30.4
Balance of payments	(millions of U.S. dollars)			
Merchandise exports (f.o.b.)	21.4	17.4	19.0	18.6
Merchandise imports (c.i.f.)	-49.3	-57.5	-63.1	-71.3
Travel (net)	12.0	13.3	10.0	9.7
Other services and private transfers (net)	10.7	13.5	10.9	7.3
Balance on current and transfer accounts	-5.2	-13.3	-23.2	-35.7
Official capital (net) including grants	9.3	14.0	20.3	23.8
Private capital (net) and errors and omissions	-5.7	-1.1	-5.1	12.0
IMF transactions 2/	0.8	0.5	0.4	--
Change in official net reserves (increase -)	0.8	-0.1	7.6	-0.1

1/ In relation to liabilities to the private sector (deposits of residents, nonresidents, and statutory bodies in commercial banks) at the beginning of the period.

2/ Consists of SDR allocation and profit distribution from IMF gold sales, and gold restitution profits.

3/ Refers to Fund's holdings related to credit tranche (including SBA) and EFF purchases from Fund resources, plus purchases from Supplementary and Enlarged Access resources.

Grenada: Summary of Financial Program for 1983/84

I. Major Assumptions

1. Real GDP is expected to grow by 2.3 per cent reflecting a pickup in agricultural output, exports, tourism, and manufacturing; allowance has been made for the effects of a slowdown in government services and public construction.

2. The velocity of M2 (money and quasi-money) is expected to remain unchanged in 1983/84.

3. The local private banks are assumed to build up their liquid assets to about 8 per cent of their deposit liabilities by the end of June 1984.

II. Targets

1. Domestic inflation is projected to decline to 7 per cent from 7.5 per cent in the preceding year.

2. The deficit in the current account of the balance of payments is projected to decline to 26.7 per cent of GDP from 30.7 per cent in the preceding year.

3. The ratio of net foreign assets to total deposits of the government-owned commercial banks is projected to rise from 2.5 per cent at the end of June 1983 to 10 per cent by the end of June 1984.

III. Principal Elements of the Program

1. Fiscal policy

The overall deficit of the nonfinancial public sector is projected to fall to 27.5 per cent of GDP in 1983/84 from 33.4 per cent in the preceding year; this reduction reflects an increase in the nonfinancial public sector savings from 2.9 per cent to 3.5 per cent of GDP, and a reduction in the ratio of capital spending to GDP from 35.7 per cent to 31 per cent. After receipts of external grants and concessionary loans, the deficit that remains is expected to decline to 7 per cent of GDP from 11.5 per cent in the preceding year.

The National Insurance Scheme, instituted in April 1983, is projected to generate a surplus of EC$5 million in 1983/84, and the nonfinancial public enterprises are expected to achieve a current account surplus of EC$2 million in the first year of the program compared with EC$1 million in the pre-program year. However, central government savings are projected to decline by EC$3.3 million to EC$4.7 million, mainly because the rising wage and interest payments are expected to be only partially offset by the recent introduction of a tax package with expected annual yield of EC$4.2 million (1.3 per cent of GDP); the effects of the tight wage policy, which involves an increase in the wage bill of only 5-1/2 per cent a year from January 1984, will be felt in the latter part of the first program year.

2. Money and credit

The Central Government will reduce its outstanding debt to local commercial banks by EC$5.9 million during 1983/84, and there will be no net bank borrowing by the rest of the public sector. The 20 per cent special deposit requirements applied to the local commercial banks will be reduced by 1 percentage point a quarter in the first year of the program.

The reduction of this deposit requirement, together with the projected increase of about 6.5 per cent in total commercial bank deposits, will allow for the buildup of bank liquidity to about 10 per cent of total deposits and a growth of about 12 per cent in bank lending to the private sector.

3. External sector

Banana and cocoa export prices are expected to lead the pickup of about 9 per cent in average export prices in the first program year; the volume of exports is forecast to increase by about 4 per cent. The unit value of imports is assumed to remain unchanged while the volume of imports is forecast to rise by 5.4 per cent, or somewhat more than GDP, due mainly to a 9.7 per cent increase in government imports for the public sector investment program. Continuing the upturn observed in the first quarter of 1983, the number of tourist arrivals is projected to rise by 9.2 per cent in the first program year; the daily expenditure per visitor is projected to rise by 1.7 per cent. The external debt service is projected to rise by about 3 percentage points to 7.7 per cent of receipts from exports, services, and private transfers, reflecting the rise in debt, particularly the nonconcessional loans, contracted in the first 12 months.

Grenada: Selected Economic and Financial Indicators, 1981-86

	Actual 1981	Prel. 1982	Est.1/ 1982/83	Program 1/ 1983/84	1984/85	1985/86
(Annual per cent changes, unless otherwise specified)						
National income and prices						
GDP at constant prices	3.4	3.3	3.0	2.3	3.0	5.0
GDP deflator	9.6	7.5	7.3	7.0	7.3	7.7
Consumer prices (average)	18.8	7.8	7.5	7.0	6.9	6.8
External sector (on the basis of U.S. dollars)						
Exports, f.o.b.	9.1	-2.1	2.4	13.3	10.9	18.0
Imports, c.i.f.	9.7	13.0	-0.7	5.8	3.8	15.2
Terms of trade (deterioration -)	-13.4	-7.7	-3.1	9.2	3.6	1.9
Nominal effective exchange rate (depreciation -)	12.5	9.4	8.2	...	...	...
Real effective exchange rate (depreciation -)	20.3	9.9	9.7	...	...	...
Public sector						
Revenue	5.4	20.9	19.6	16.6	14.4	13.3
Grants and concessionary loans (net)	44.6	8.9	13.3	5.7	-5.1	-2.5
Total expenditure and net lending	44.2	21.6	14.6	3.3	-6.0	8.2
Money and credit 2/						
Domestic credit (net)3/	2.3	24.5	6.9	3.3	4.0	8.8
Central Government 3/	(1.0)	(20.3)	(1.9)	(-4.6)	(-3.7)	(-1.9)
Rest of public sector	(2.0)	(2.6)	(2.3)	(0.2)	(0.7)	(0.7)
Private sector 3/	(2.4)	(5.3)	(3.0)	(7.7)	(7.0)	(9.3)
Bank liabilities to private sector (M2)	6.6	5.0	7.1	9.1	9.7	12.2
Velocity (GDP relative to M2)4/	1.5	1.6	1.7	1.7	1.7	1.7
Interest rate (annual rate, one-year savings deposit)4/	5.0	5.0	5.0	5.0	5.0	5.0
(In per cent of GDP)						
Public sector						
Savings	-0.7	2.7	2.9	3.5	4.6	5.7
Overall deficit	-30.7	-33.4	-32.7	-27.5	-18.2	-16.2
Overall deficit after grants	-17.2	-17.9	-17.8	-14.9	-10.9	-8.5
Overall deficit after external grants and concessionary loans	-9.5	-12.9	-11.5	-7.0	-0.5	-0.8
Gross domestic investment	33.5	38.3	38.0	34.6	28.1	28.8
Gross national savings	9.3	5.1	7.3	7.9	10.4	12.3
BOP-Current account balance 5/	-24.2	-33.2	-30.7	-26.7	-17.7	-16.5
BOP-Current account balance	-10.7	-17.7	-15.7	-14.2	-10.5	-8.8
External debt (excluding IMF)	17.9	22.2	31.1	41.3	48.0	50.4
External debt (including IMF)	26.5	28.7	37.1	50.5	58.2	61.0
(In per cent of receipts from exports, services, and private transfers)						
Debt service (including IMF)6/	2.7	4.5	4.6	7.7	12.2	12.6
Interest payments (including IMF)6/	1.3	1.6	2.5	4.0	4.9	5.0
(In millions of SDRs, unless otherwise specified)						
Overall balance of payments	-6.4	0.1	-0.7	-4.2	-2.4	-2.1
Gross official reserves (weeks of imports)7/	9.4	5.8	5.4	5.1	5.6	5.4
External payments arrears	--	--	--	--	--	--

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

1/ Year beginning July 1.
2/ Refers to commercial banks only.
3/ Changes in relation to M2 at the beginning of period.
4/ M2 includes bank liabilities to private sector and currency in circulation.
5/ Before official grants.
6/ Does not take into account the decline in the domestic debt burden (including to ECCA) under the proposed program.
7/ Includes an imputed share of ECCA international reserves.

Grenada: Extended Arrangement

Attached hereto is a letter dated , 1983 from the Minister of Planning, Finance and Trade of Grenada requesting an extended arrangement and setting forth:

(a) the objectives and policies that the authorities of Grenada intend to pursue for the period of the extended arrangement;

(b) the policies and measures that the authorities of Grenada intend to pursue for the first year of the extended arrangement; and

(c) understandings of Grenada with the Fund regarding reviews that will be made of progress in realizing the objectives of the program and of the policies and measures that the authorities of Grenada will pursue for the second and third years of the extended arrangement.

To support these objectives and policies the International Monetary Fund grants this extended arrangement in accordance with the following provisions:

1. For a period of three years from , 1983, Grenada will have the right to make purchases from the Fund in an amount equivalent to SDR 13.5 million, subject to paragraphs 2, 3, 4, and 5 below, without further review by the Fund.

2. (a) Until July 31, 1984, purchases under this arrangement shall not, without the consent of the Fund, exceed the equivalent of SDR 4,500,000, provided that purchases shall not exceed the equivalent of SDR 1,125,000 until November 15, 1983, the equivalent of SDR 2,250,000 until February 15, 1984, and the equivalent of SDR 3,375,000 until May 15, 1984.

(b) Until July 31, 1985, purchases under this arrangement shall not, without the consent of the Fund, exceed the equivalent of SDR 9,000,000.

(c) The right of Grenada to make purchases during the second and third years shall be subject to such phasing as shall be determined.

3. Purchases under this arrangement shall be made from borrowed resources until purchases under this arrangement reach the equivalent of SDR 1,775,000; thereafter, purchases under this arrangement shall be made from ordinary and borrowed resources in the ratio of 1 to 1 until purchases under the arrangement reach the equivalent of SDR 10,825,000; and thereafter, purchases shall be made from borrowed resources only; provided that any modification by the Fund of the proportions of ordinary and borrowed resources shall apply to amounts that may be purchased after the date of modification.

4. Grenada will not make purchases under this arrangement:

(a) through July 31, 1984, during any period in which the data at the end of the preceding period indicate that

(i) the limits on nonconcessional financing specified in paragraph 14 of the attached letter dated , 1983, or

(ii) the limits on the liquid assets of the state banks as specified in paragraph 15 of the attached letter dated , 1983 are not observed; or

(b) if Grenada fails to observe the limit on contracting or guaranteeing of foreign loans and borrowing from ECCA specified in paragraph 14 of the attached letter dated , 1983; or

(c) after January 31, 1984, until the review contemplated in paragraph 17 of the attached letter dated , 1983 has been completed or understandings reached under this review are being observed; or

(d) for the period from August 1, 1984 through July 31, 1985 and from August 1, 1985 through July 31, 1986, if before August 1, 1984 and August 1, 1985, respectively, suitable performance clauses for these periods have not been established in consultation with the Fund as contemplated in paragraph 17 of the attached letter dated , 1983 or if such clauses, having been established, are not being observed; or

(e) throughout the duration of the arrangement, if Grenada

(i) imposes restrictions on payments and transfers for current international transactions, or

(ii) introduces new, or modifies existing, multiple currency practices, or

(iii) concludes bilateral payments agreements which are inconsistent with Article VIII, or

(iv) imposes or intensifies import restrictions for balance of payments reasons.

When Grenada is prevented from purchasing under this arrangement because of this paragraph 4, purchases will be resumed only after consultation has taken place between the Fund and Grenada and understandings have been reached regarding the circumstances in which such purchases can be resumed.

5. Grenada's right to engage in the transactions covered by this arrangement can be suspended only with respect to requests received by the Fund after (a) a formal ineligibility, or (b) a decision of the Executive Board to suspend transactions, either generally or in order to consider a proposal, made by an Executive Director or the Managing Director, formally to suppress or to limit the eligibility of Grenada. When notice of a decision of formal ineligibility or of a decision to consider a proposal is given pursuant to this paragraph 5, purchases under this agreement will be resumed only after consultation has taken place between the Fund and Grenada and understandings have been reached regarding the circumstances in which such purchases can be resumed.

6. Purchases under this arrangement shall be made in the currencies of other members selected in accordance with the policies and procedures of the Fund, and may be made in SDRs if, on the request of Grenada, the Fund agrees to provide them at the time of the purchase.

7. The value date of a purchase under this extended arrangement involving borrowed resources will be normally either the 15th day or the last day of the month, or the next business day if the selected day is not a business day. Grenada will consult the Fund on the timing of purchases involving borrowed resources.

8. Grenada shall pay a charge for this arrangement in accordance with the decisions of the Fund.

9. (a) Grenada shall repurchase the amount of its currency that results from a purchase under this extended arrangement in accordance with the provisions of the Articles of Agreement and decisions of the Fund, including those relating to repurchase as Grenada's balance of payments and reserve position improves.

(b) Any reductions in Grenada's currency held by the Fund shall reduce the amounts subject to repurchase under (a) above in accordance with the principles applied by the Fund for this purpose at the time of the reduction.

(c) The value date of a repurchase in respect of a purchase financed with borrowed resources under this extended arrangement will be normally either the 6th day or the 22nd day of the month, or the next business day if the selected day is not a business day, provided that repurchase will be completed not later than seven years from the date of purchase.

10. During the period of the arrangement Grenada shall remain in close consultation with the Fund. These consultations may include correspondence and visits of officials of the Fund to Grenada or of representatives of Grenada to the Fund. Grenada shall provide the Fund, through reports at intervals or dates requested by the Fund, with such information as the Fund requests in connection with the progress of Grenada in achieving the objectives and policies set forth in the attached letter.

11. In accordance with paragraph 17 of the attached letter Grenada will consult the Fund on the adoption of any measures that may be appropriate at the initiative of the Government or whenever the Managing Director requests consultation because any of the criteria under paragraph 4 above have not been observed or because he considers that consultation on the program is desirable. In addition, after the period of the arrangement and while Grenada has outstanding purchases under this arrangement, the Government will consult with the Fund from time to time, at the initiative of the Government or at the request of the Managing Director, concerning Grenada's balance of payments policies.

Ministry of Planning,
Finance and Trade
St. George's
Grenada, W.I.
August , 1983

Mr. Jacques de Larosiere
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Mr. de Larosiere:

1. The Government of Grenada hereby requests a three-year Extended Arrangement with the International Monetary Fund for an amount equivalent to SDR 13.5 million, including amounts from ordinary resources and from borrowed resources.

2. Despite the world recession and adverse publicity abroad, the Grenadian economy has expanded by an annual average of over 3 per cent in the last three years, led by construction of basic infrastructure, the main element of the public investment programme. The growth of real GDP is expected to slow down slightly to about 2-1/2 per cent in 1983. The rise in consumer prices dropped to 7-3/4 per cent in 1982 from an annual average of 20 per cent in the preceding two years; in the 12 months through April 1983, the consumer price index rose by only 5-1/2 per cent. These price developments reflected mainly the deceleration in import prices, but also increased competition in the domestic market from the operations of the state-owned Marketing and National Importing Board (MNIB), and some moderation in the growth of nominal wages.

3. Grenada's deficit in the current account of the balance of payments widened to US$35.7 million in 1982, which was the equivalent of over 33 per cent of GDP, up from 7 per cent of GDP in 1979, due to adverse movements in the terms of trade, a decline in tourist arrivals, and a rise in imports related to investment spending. In the last three years, the current deficits have been financed mostly by external grants and concessional loans, but also in part by borrowing from the Fund and, in 1982, by a reduction in the commercial banks' foreign assets following an increase in the special deposit requirement. External debt and debt service has risen moderately in recent years; most of the debt has been on concessional terms.

4. Improved expenditure controls and revenue administration have helped to make possible a considerable fiscal adjustment over the last four years. By 1982, central government savings amounted to EC$8 million, compared with a deficit of EC$4 million in 1978. The Government's policy is to generate local savings in order to contribute to the investment effort.

5. The Government of Grenada is engaged in a major effort of structural transformation, requiring heavy investments in economic infrastructure. To that end public investment outlays, which had averaged only about 7.5 per cent of GDP a year between 1975 and 1978, have been raised to the equivalent of over 24 per cent of GDP a year in the four succeeding years. Of the investment outlays in the last four years, approximately 53 per cent was covered by external grants, 18 per cent by net foreign concessional loans, 2 per cent by nonconcessional foreign borrowing and the remainder from other sources, including borrowing from local banks and insurance companies and the Fund. Some 42 per cent of total public investment outlays during these four years has been on a new international airport which will be completed in the first half of 1984. In addition, 20 per cent has been spent on other productive infrastructure over the same period, including roads, water, electricity and telephone services, and port facilities.

6. The Government of Grenada is committed to the achievement of economic development and social transformation through the joint effort of the public and private sectors. Private sector investment, both local and foreign, is particularly welcome in the manufacturing and tourist sectors of the economy. Through its investment programme and other policies, the Government is creating modern transportation and communication links internationally, and improving the stock of economic and social infrastructure. The Government believes that a skilled and healthy labor force, an environment of good industrial relations, and the growing consciousness of workers of the need to relate wage demands to their own productivity and enterprises' ability to pay have helped to create a favorable investment climate. In addition, the new investment code, approved by the Cabinet in April 1983, encourages domestic and foreign investment, especially in manufacturing and tourism, and provides a range of fiscal and other incentives. The improved investment climate is reflected in increased applications for loans from the GDB and CDB by the private sector, especially for tourism-related investments. Applications for fiscal incentives have shown an upward trend since 1981, especially in the first half of 1983.

7. The state-owned Marketing and National Importing Board (MNIB) acts as an outlet in the domestic and external markets for agricultural produce and processed foods, and as an importer of basic commodities. By importing in bulk from traditional and nontraditional sources, the MNIB seeks to obtain the most favorable prices and to provide stability to domestic prices. Presently the MNIB is the sole importer of rice, sugar, milk powder, and cement and engages in imports of fertilizer and

tires. The Government has announced that over the next three years the MNIB will not be granted any import monopolies. However, MNIB will be able to import any product in competition with private importers, and subject to the same regulations as regards payment of duties or taxes, and import licensing.

8. The Government has always given high priority to increasing production in the agricultural sector. The Grenada Farms Corporation (GFC) has increased the number of acres under cultivation and is giving urgent attention to upgrading all aspects of its operations, especially marketing, farm management, and technology. During the first quarter of 1983, GFC farms have been organized into seven units (comprising three or four farms each) with a technically qualified person managing each unit. Additionally, agro-technical and management training is being provided on an ongoing basis to all levels of GFC staff.

9. The program in support of which we are requesting Fund assistance has as its main objective a reduction in the financial imbalances in the economy, achievement of a viable balance of payments position, and at the same time completion of the programme of investments necessary for generating sustainable growth. Over the programme period the Government plans to raise further the level of public sector savings, and reduce the public sector overall deficit in relation to GDP, especially the use of nonconcessionary financing so as to ensure that the capacity of the economy to service its debt is preserved.

10. The main parameters of our three-year programme are shown in Table 1 (annexed). The fiscal programme for the programme year 1983/84 (year ending June 30) is annexed in Table 2, which also provides estimates for the two subsequent programme years.

11. In order to strengthen Central Government savings, the Government recently implemented new revenue measures consisting of an increase in the airport levy from 2 per cent to 5 per cent, an increase in the motor vehicle tax from 30 per cent to 40 per cent, and adjustments in government fees and charges, which are expected to raise EC$4.2 million during the first year of the programme. In addition, the increase in the wage bill of the Central Government will be at least 1 percentage point below the expected rate of inflation during the programme period. Wage policy in the rest of the public sector will be designed to achieve the operating surpluses projected under the programme.

12. The operations of the rest of the public sector, including the National Insurance Board (NIB) and 11 selected enterprises for which programmes have been prepared, will provide a major increase in savings over the programme period. The National Insurance Scheme which started operations in April 1983 and is based on contributions of 4 per cent of wages each from employer and employee, is expected to generate resources equivalent to 1.5 per cent of GDP in its first full year of operations. With respect to the state enterprises, it is Government's policy not to subsidize their current operations. Social services such as the National

Transport Service are expected to cover their operating costs; others are expected to make adequate profits so as to mobilize resources for the development effort. Utilities' tariffs will be adjusted as necessary so that the operating surpluses of these enterprises will be adequate to cover debt service, and to provide a reasonable rate of return on capital.

13. The Government plans to carry out a review of the tax structure with a view to effecting reforms over the next few years, and we have requested technical assistance for the conduct of this review. Within the framework of these reforms, the Government will reduce the existing tax on foreign exchange transactions over time, in order to harmonize our practice with that in the majority of member countries of ECCA. In the meantime, and pending the identification and adoption of alternative taxes, we request a continuation of approval by the Fund of the 5 per cent tax on foreign exchange transactions, which was imposed for budgetary purposes and constitutes a multiple currency practice.

14. The cumulative use of nonconcessional financing of the public sector as defined in Annex 1 will not exceed EC$6.8 million between July 1, 1983 and September 30, 1983, EC$14.6 million between July 1, 1983 and December 31, 1983, EC$19.5 million between between July 1, 1983 and March 31, 1984, and EC$23.6 million between July 1, 1983 and June 30, 1984. These limits include provision for EC$16.8 million of nonconcessional foreign borrowing disbursed in equal quarterly installments: the limits will be automatically modified as required in case of any deviation from this schedule of disbursements for these specific loans. Apart from these loans, which have already been contracted, the Government will not contract or guarantee any further foreign borrowing on nonconcessional terms during the programme period without reaching agreement with the Fund. To the extent that the Government utilizes any borrowing margin that may accrue to it in ECCA (soon to be established as the regional central bank), this will be added to the liquid reserves of the two state-owned banks (the NCB and GBC) over and above the amounts specified in paragraph 15. The public sector will reduce its outstanding debt to the domestic banking system by at least EC$5.9 million in the first year of the programme, by EC$5.0 million in the second year, and by EC$2.9 million in the third year.

15. The Government has set targets to rebuild the liquid assets of the state banks (the NCB and GBC) to 10 per cent of their deposit liabilities by the end of June 1984, 18 per cent by the end of June 1985 and 20 per cent one year later. Accordingly, the liquid assets of the state banks will be no less than EC$2.5 million at the end of September 1983, EC$3.9 million at the end of December 1983, EC$5.3 million at the end of March 1984 and EC$6.7 million at the end of June 1984. The financing plan for the public sector outlined in paragraph 14 and in the attached Table 2, also implies that net outstanding bank credit to the rest of the public sector from the state banks, and to the total public sector from private commercial banks will remain level over the programme period. Therefore, the 20 per cent special deposit requirement will be

reduced by 1 percentage point per quarter during the first programme year and further in subsequent years. This credit programme is expected to result in a growth of loanable resources adequate to support an expansion of private sector productive activities and investment during the programme period, while at the same time strengthening the financial position of the state banks.

16. The 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 in relation to known development priorities. In pursuing this objective the Government will consult with other member governments of the Eastern Caribbean Central Bank soon to be established on a coordinated regional interest rate strategy. Also, in view of the fact that over the past two years the trade-weighted exchange rate of the East Caribbean dollar has appreciated markedly, particularly for Grenada, the Government will review with other member governments of the Eastern Caribbean Central Bank the regional exchange rate level and system at an early opportunity.

17. The Government of Grenada will reach agreement with the Fund by July 31, 1984 on a financial programme to cover the programme year ending June 30, 1985, and by July 31, 1985 on a financial programme to cover the remaining year of the arrangement. The Government of Grenada will also review with the Fund by January 31, 1984 the progress made in implementing the fiscal programme in Table 2. While recognizing the importance of implementing fully the programme outlined above, the Government also hopes that favorable consideration can be given to an increase in the use of Fund resources during the programme period if Fund policies on access are modified, and to the possible utilization of any SDR allocation, if there were to be one.

18. The Government of Grenada believes that the policies set forth in this letter are adequate to achieve the objectives of its programme but will take any further measures that may be appropriate for this purpose. The Government of Grenada will consult with the Fund on the adoption of any measures that may be appropriate, in accordance with the policies of the Fund on such consultations.

Sincerely yours,

Bernard Coard
Minister of Finance, Planning
and Trade

Annexed: Technical Memorandum of Understanding

Table 1. Grenada: Principal Parameters

	Average 1979-80	1981	Prel. 1982	Est. 1/ 1982/83	Projections 1/ 1983/84	1984/85	1985/86
	(Percentage changes)						
Real GDP	2.5	3.4	3.3	3.0	2.3	3.0	5.0
Nominal GDP	16.1	11.5	12.2	11.4	9.6	9.9	12.2
Nominal domestic expenditure	24.4	15.7	18.7	12.1	6.1	3.1	12.0
Consumer prices (average)	20.6	18.8	7.8	7.5	7.0	6.9	6.8
	(Ratios to GDP)						
Balance of payments							
Current account deficit	-11.2	-24.2	-33.2	-30.7	-26.7	-17.7	-16.5
Official grants	12.1	13.5	15.5	14.9	12.6	7.2	7.7
Overall balance	-1.6	-7.9	0.1	-0.6	-3.7	-1.9	-1.5
National accounts							
Consumption	104.2	99.7	102.6	100.3	99.3	97.4	96.6
Public sector	(24.7)	(24.5)	(22.0)	(18.7)	(18.5)	(19.2)	(17.7)
Private sector	(79.5)	(75.2)	(80.6)	(81.6)	(80.8)	(78.2)	(78.9)
Investment	19.0	33.5	38.3	37.9	34.6	28.1	28.8
Public sector	(14.4)	(30.3)	(34.8)	(35.6)	(31.0)	(22.7)	(21.9)
Private sector	(4.6)	(3.2)	(3.5)	(2.3)	(3.6)	(5.4)	(6.9)
Gross domestic savings	-4.2	0.3	-2.6	-0.3	0.7	2.5	3.4
Public sector finances							
General government current surplus	- 0.22	-0.4	2.3	2.6	2.9	3.9	5.1
Current revenue	(25.9)	(24.2)	(25.5)	(26.8)	(28.2)	(29.3)	(29.7)
Current expenditure	(26.1)	(24.7)	(23.2)	(24.2)	(25.3)	(25.4)	(24.6)
Current surplus of the rest of public sector	0.2	-0.3	0.4	0.3	0.6	0.6	0.6
Public sector current surplus	—	-0.7	2.7	2.9	3.5	4.6	5.7
Public sector capital expenditures	15.2	30.1	36.1	35.7	31.0	22.7	21.9
Overall deficit	-15.0	-30.7	-33.4	-32.7	-27.5	-18.2	-16.2
Overall deficit (after grants)	-3.0	-17.2	-17.9	-17.8	-14.9	-10.9	-8.5
Nonconcessional financing	0.7	9.5	12.9	11.5	7.0	0.5	0.8

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

1/ Refers to year beginning July 1.

Table 2. Grenada: Summary Public Sector Operations

	1979	1980	1981	Prel. 1982	Est.1/ 1982/83	Program 1/ 1983/84	Program 1/ 1984/85	Program 1/ 1985/86
	(In millions of East Caribbean dollars)							
Current balance	0.9	-0.8	-1.9	7.7	9.0	11.7	16.8	23.5
Central Government	1.0	-2.1	-1.1	7.7	8.0	4.7	9.0	14.9
Current revenue	(54.9)	(57.5)	(62.7)	(74.2)	(81.9)	(89.7)	(102.8)	(116.7)
Current expenditure	(53.9)	(59.6)	(63.8)	(67.5)	(73.9)	(85.0)	(93.8)	(101.8)
National Insurance Scheme	--	--	--	--	--	5.0	5.5	6.0
Nonfinancial public enterprises	-0.1	1.3	-0.8	1.0	1.0	2.0	2.3	2.6
Capital receipts	0.2	0.2	0.3	--	--	--	--	--
Capital expenditures	27.6	38.7	77.9	104.8	109.0	103.9	83.8	90.4
Of which: airport	(10.1)	(21.0)	(34.3)	(46.2)	(64.6)	(40.0)	(0.4)	(--)
contingency fund	(--)	(--)	(--)	(--)	(--)	(1.0)	(1.7)	(3.3)
Overall balance	-26.5	-39.3	-79.5	-97.1	-100.0	-92.2	-67.0	-66.9
External grants	18.6	34.4	34.9	45.0	45.5	42.1	26.8	31.8
Overall balance after grants	-7.9	-4.9	-44.6	-52.1	-54.5	-50.1	-40.2	-35.1
External concessionary loans (net)	6.4	3.5	19.9	14.7	19.4	26.5	38.3	31.7
Overall balance after grants and concessionary loans	-1.5	-1.4	-24.7	-37.4	-35.1	-23.6	-1.9	-3.4
Nonconcessional financing	1.5	1.4	24.7	37.4	35.1	23.6	1.9	3.4
Commercial loans (external)	--	--	--	4.4	21.9	16.8	--	--
Change in foreign assets	-0.2	-1.1	2.7	--	--	2.4	--	--
SDR allocation	1.1	1.1	1.1	--	--	--	--	--
Net IMF purchases	1.2	--	15.6	-2.4	-2.0	12.3	6.9	6.3
Net ECCA borrowing	1.0	0.9	2.2	2.2	2.2	--	--	--
Net domestic borrowing	-1.6	0.5	3.1	33.2	13.0	-7.9	-5.0	-2.9
Commercial banks	(-2.8)	(-4.8)	(3.7)	(29.9)	(5.0)	(-5.9)	(-5.0)	(-2.9)
Nonbanks	(2.2)	(1.8)	(3.4)	(3.9)	(7.5)	(-2.0)	(--)	(--)
Residual	(-1.0)	(3.5)	(-4.0)	(-0.6)	(0.5)	(--)	(--)	(--)

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

1/ Year ending in June.

Table 3. Grenada: Balance of Payments

	1979	1980	1981	1982	Est. 1/ 1982/83	Projections 1/ 1983/84	1984/85	1985/86
	(In millions of U.S. dollars)							
Current account	-5.2	-13.3	-23.2	-35.7	-34.8	-33.2	-24.2	-25.2
Goods and services	-13.2	-26.1	-37.8	-50.1	-49.1	-47.7	-40.7	-42.7
Merchandise trade	-27.9	-40.1	-44.1	-52.7	-52.9	-54.5	-55.0	-62.7
Exports, f.o.b.	(21.4)	(17.4)	(19.0)	(18.6)	(19.5)	(22.1)	(24.5)	(28.9)
Imports, c.i.f.	(-49.3)	(-57.5)	(-63.1)	(-71.3)	(-72.4)	(-76.6)	(-79.5)	(-91.6)
Of which: airport related	/2.4/	/4.7/	/6.2/	/8.8/	/12.9/	/9.6/	/0.2/	/--/
Services	14.7	13.4	6.3	2.6	3.8	6.8	14.3	20.0
Travel receipts	(15.3)	(16.5)	(13.9)	(13.0)	(13.7)	(16.1)	(21.1)	(27.0)
Travel payments	(-3.3)	(-3.2)	(-3.9)	(-3.3)	(-3.4)	(-4.0)	(-4.2)	(-5.6)
Interest of public debt	(-0.4)	(-0.4)	(-0.6)	(-0.8)	(-1.4)	(-2.5)	(-3.5)	(-4.3)
ECCA profits	(0.5)	(0.7)	(0.8)	(1.1)	(1.1)	(1.1)	(1.2)	(1.3)
Other services (net)	(2.6)	(-0.2)	(-3.9)	(-7.4)	(-6.2)	(-3.9)	(0.2)	(1.2)
Private transfers (net) 2/	8.0	13.4	14.6	14.4	14.3	14.5	16.5	17.5
Capital account	6.2	13.7	18.1	33.8	35.3	28.6	21.6	22.9
Public sector grants	6.9	12.7	12.9	16.7	16.9	15.6	9.9	11.8
Public sector borrowing (net)	2.4	1.3	7.9	7.1	15.3	16.0	14.2	11.7
Commercial banks (net)	-1.1	1.1	-0.8	9.4	3.3	-2.2	-2.4	-1.3
Private investment	--	--	--	1.9	1.4	1.0	1.9	3.1
Currency holdings 3/	-2.0	-1.4	-1.4	-1.3	-1.6	-1.8	-2.0	-2.4
Errors and omissions	-2.6	-0.8	-2.9	2.0	-1.2	--	--	--
SDR allocations 4/	0.8	0.5	0.4	--	--	--	--	--
Overall surplus or deficit (-)	-0.8	0.1	-7.6	0.1	-0.7	-4.6	-2.6	-2.3
Financing	0.8	-0.1	7.6	-0.1	0.7	4.6	2.6	2.3
IMF (net)	0.5	--	6.0	-0.9	-0.8	4.6	2.6	2.3
ECCA borrowing	0.4	0.3	0.8	0.8	0.7	--	--	--
Government foreign assets	-0.1	-0.4	1.0	--	0.8	--	--	--
	(In per cent of GDP)							
Current balance	-6.9	-15.5	-24.2	-33.2	-30.7	-26.7	-17.7	-16.5
Excluding airport	(-3.7)	(-10.0)	(-17.7)	(-25.0)	(-19.3)	(-17.7)	(-17.6)	(-16.5)
Overall balance	-2.0	-1.1	-7.9	0.1	-0.6	-3.7	-1.9	-1.5
Memorandum items								
Banana exports ('000 tons)	14.1	12.5	10.2	9.8	10.3	10.6	11.1	12.3
Cocoa exports ('000 tons)	2.4	1.9	2.7	2.1	2.4	2.5	2.7	2.9
Nutmeg exports ('000 tons)	2.3	1.5	1.7	2.1	2.7	2.5	2.6	2.8
Stayover visitors ('000)	32.3	29.4	25.1	23.2	24.2	26.5	30.9	36.3
Debt service ratio 5/	3.7	3.0	2.7	4.5	4.6	7.7	12.2	12.6

Sources: Ministry of Planning, Finance and Trade; Statistical Office; and Fund staff estimates.

1/ Refers to year beginning July.
2/ Includes migrant transfers, workers' remittances, other transfers from Grenadians living abroad, and medical students transfers for expenses not covered by payments made abroad to the school.
3/ East Caribbean dollars in circulation.
4/ Includes profits from gold sales.
5/ Interest and amortization as per cent of receipts from exports, services, and private transfers.

Technical Memorandum of Understanding

In paragraph 14, nonconcessional financing is defined to include any nonconcessional external loans (using the annexed World Bank definition but excluding loans from CDB and OPEC), changes in government sinking fund balances, net borrowing from IMF, SDR allocations, net borrowing from ECCA, and net borrowing from local commercial banks, nonbanks, insurance companies, and other domestic sources.

In paragraph 14, the rest of the public sector is defined to include the National Insurance Scheme and all nonfinancial state enterprises and statutory bodies but excluding Grenada Cocoa Association, Grenada Nutmeg Association, Banana Growers' Association, and Minor Spices Cooperative Society which are basically farmers cooperatives, with some government participation, operating on a commercial basis (external loans of these cooperatives are included in the public sector).

In paragraph 15, bank liabilities for the liquid assets ratio are defined to include all deposits from the private sector, nonresidents and public sector, excluding the Central Government. The liquid assets of commercial banks are defined as cash, balances due from ECCA, balances due from ECCA area banks other than in territory, balances due from banks abroad less borrowing and balances due to ECCA, balances due to ECCA area banks other than in territory, and balances due to banks abroad (ECCA Form B.S. 1 revised).

For the programme period an accounting rate of US$1.09 per SDR has been used.

Maximum Interest Rate Compatible with Concessional Loans 1/

(In per cent)

Years to Maturity	Grace Period (In years) 1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
1	...														
2	...	...													
3	...	...	...												
4	...	0.56	1.64	2.06											
5	0.45	1.58	2.41	3.06	3.32										
6	1.46	2.35	3.02	3.55	3.98	4.16									
7	2.23	2.95	3.51	3.95	4.31	4.62	4.75								
8	2.83	3.43	3.90	4.28	4.60	4.86	5.09	5.19							
9	3.32	3.83	4.23	4.56	4.84	5.07	5.27	5.45	5.52						
10	3.72	4.16	4.51	4.80	5.05	5.26	5.44	5.59	5.73	5.79					
11	4.06	4.44	4.75	5.01	5.23	5.42	5.58	5.72	5.84	5.95	6.00				
12	4.34	4.68	4.95	5.19	5.39	5.56	5.70	5.83	5.95	6.05	6.14	6.18			
13	4.58	4.88	5.13	5.34	5.52	5.68	5.82	5.93	6.04	6.13	6.22	6.29	6.33		
14	4.79	5.06	5.29	5.48	5.65	5.79	5.91	6.03	6.12	6.21	6.29	6.36	6.42	6.45	
15	4.98	5.22	5.43	5.60	5.76	5.89	6.00	6.11	6.20	6.28	6.35	6.42	6.47	6.53	6.55

Source: IBRD, Grant Element Tables.

1/ According to the DAC definition that defines as concessional those loans with a grant element in excess of 25 per cent on the basis of a 10 per cent rate of discount.

For the purpose of this table, loans are assumed to be repaid in equal semiannual installments of principal. Grace period is defined as the interval to first repayment, minus one payment period.

This table shows the maximum rate a loan can have and still meet the DAC criterion for concessional loans. For example, a ten-year loan with five years of grace would be concessional if the interest rate is less or equal to 5.05 per cent, but would fail the criterion at higher rates.