

MASTER FILES

ROOM C-120

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SM/85/278
Correction 1

CONTAINS CONFIDENTIAL
INFORMATION

October 31, 1985

To: Members of the Executive Board
From: The Secretary
Subject: Vanuatu - Staff Report for the 1985 Article IV Consultation

The following corrections have been made in SM/85/278 (10/7/85):

Page 3, Table 1, last column, 5th line from bottom: for "-6.1" read "-6.4"
penultimate line: for "2.6" read "4.1"

Page 6, Table 2, last column,
lines 9, 10, 11, and 13: for "2,980" read "1,938"
for "10,327" read "11,369"
for "(17.4)" read "(29.2)"
for "8,168" read "9,210"

Page 10, Table 4, column 5, Total expenditure: for "5,228.2" read "5,306.2"
Other 2/: for "231.9" read "309.9"
Domestic (net) 3/: for "-431.4" read "-434.1"

Page 19, Basic Data: revised

Corrected pages are attached.

Att: (4)

Other Distribution:
Department Heads

Table 1. Vanuatu: Balance of Payments, 1982-85

(In millions of SDRs)

	1982	1983	1984	1985 Est.
Trade balance	-29.9	-25.8	-19.2	-33.5
Exports (f.o.b.)	9.7	16.8	30.8	17.1
Of which: copra	(6.7)	(12.3)	(26.0)	(13.0)
Imports (f.o.b.)	39.6	42.6	50.0	50.6
Of which: for home consumption	(35.9)	(40.2)	(47.1)	(47.5)
Sources and transfers (net)	39.8	29.0	38.2	28.1
Services (net)	0.9	-1.1	-0.6	-3.3
Receipts	38.4	40.6	48.1	41.9
Of which: inward travel	(19.3)	(20.7)	(23.2)	(17.6)
Payments	37.5	41.7	48.7	45.2
Of which: investment income	(4.8)	(11.3)	(11.4)	(10.0)
Private transfers (net)	7.4	5.6	6.8	6.5
Official transfers (net)	31.5	24.5	32.0	24.9
Current account balance	9.9	3.2	19.0	-5.4
Current account balance excluding official transfers	(-21.6)	(-21.3)	(-13.0)	(-30.3)
Nonmonetary capital	5.9	7.7	8.8	11.0
Long-term capital	2.5	12.2	8.6	11.0
Official	1.4	0.3	0.7	2.8
Of which: disbursements	(1.7)	(0.6)	(1.1)	(3.0)
Private	2.7	11.9	7.9	8.2
Of which: reinvested earnings	(1.0)	(6.7)	(5.6)	(5.1)
Short-term capital	1.8	-4.5	0.2	--
Errors and omissions	0.4	5.6	11.8	--
Overall balance	16.2	16.5	39.6	5.6
Change in net foreign assets (increase -)	-16.2	-16.5	-39.6	-5.6
Monetary authorities (net)	(3.4)	(2.2)	(-5.4)	(-1.5)
Commercial banks (net)	(-19.6)	(-18.7)	(-34.2)	(-4.1)
Memorandum items:				
Current account/GDP ratio	13.4	4.1	20.5	-6.4
Current account/GDP ratio excluding official transfers	-28.6	-27.0	-14.1	-35.0
Total debt outstanding (SDRs)	3.7	3.5	3.9	6.5
Debt service ratio	5.2	3.0	1.9	4.1
Vatu/SDR (average)	106.2	106.2	101.7	107.7

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

Vanuatu's export performance improved substantially between 1982 and 1984. The value of exports (in SDR terms) rose by 73 percent in 1983 and by 83 percent in 1984 to a record SDR 31 million. However, virtually all of the increase in exports was due to larger copra earnings, which comprised 84 percent of total exports in 1984. Buoyant world prices for copra accounted for most of the gains, although export volume rose by 11 percent and 21 percent, respectively, in 1983 and 1984. The quality of copra production has also improved as a result of government efforts to improve storage facilities, replace smoke drying with the hot air drying process, and establish quality-based procurement price differentials.

Imports satisfy the bulk of monetized domestic demand. The value of imports (in SDR terms) rose by nearly 18 percent in 1984 (8 percent in 1983) to SDR 50 million. Contributing factors to this rapid expansion included much higher personal income, particularly in rural areas, generally buoyant investment activity in urban areas, and an expansion in tourism expenditures.

The current account surplus in 1984 increased sharply to SDR 19 million (20 percent of GDP), compared to only SDR 3 million (4 percent of GDP) recorded in 1983. This improvement was largely the result of a SDR 7 million reduction in the trade deficit and a SDR 6 million rise in official transfers. About half of the increase in transfers reflected STABEX grants and the U.K. contribution to a compensation fund, to meet claims arising from the 1980 civil disturbances, and were not a part of the continuing flow of assistance. Net services played only a small role in the overall outcome as increased tourist earnings were offset by larger service payments. There was a SDR 1 million gain on net private transfers, mainly owing to increased local expenditure by expatriates under technical assistance programs.

Identified capital account transactions include relatively small amounts of official long-term capital, sizable inflows of direct private capital, in most part reinvestment of earnings, and miscellaneous short-term capital items. Identified nonmonetary capital inflows in 1984 amounted to SDR 9 million, compared to SDR 8 million in 1983. As measured by monetary survey statistics, the overall balance recorded a striking surplus of SDR 39 million in 1984. The net foreign asset position of the monetary authorities (including their foreign exchange deposits with domestic commercial banks) increased by SDR 5.4 million to SDR 15.6 million at the end of 1984. The net foreign assets of the commercial banks (excluding those attributable to the monetary authorities' holdings of foreign assets noted) increased by SDR 34.2 million to SDR 78.9 million at the end of the year.

The vatu has been pegged to the SDR since September 10, 1981. In an attempt to contain pressures on domestic prices emanating from abroad, the vatu was revalued by 5.6 percent to SDR 1 = VT 100.6 on March 12, 1984. Between April 1984 and March 1985, the vatu appreciated

by 18 percent in nominal terms and 15 percent in real terms. Effective April 1, 1985, the vatu was devalued by 8.5 percent to SDR 1 = VT 110 in response to less favorable external circumstances (Chart 2).

The outstanding public external debt, incurred in part before independence, amounted to about SDR 3.9 million at the end of 1984, when debt service payments were 2 percent of merchandise exports. Since independence, the Government has negotiated about SDR 11 million in new loans mainly to supply resources to the Development Bank of Vanuatu and for agricultural projects; the bulk of these funds remain undisbursed. ^{1/} The terms of loans have been highly concessional.

Monetary developments have been dominated by the movements in the balance of payments, and growth in total liquidity in recent years has expanded at rapid rates, reflecting the large overall surpluses achieved (Table 2). The authorities' balanced budget policy has meant that the Government has not been a sustained force to expand domestic credit and credit to the private sector has been relatively moderate owing to restraints on investment. In 1984, credit to the private sector grew by only 0.2 percent; however, consumer loans fell markedly while loans for construction expanded rapidly. For the year, total domestic credit declined by 21 percent, reflecting the large overall budgetary surplus achieved. The economy has been characterized by high levels of private financial savings, reflected in the rapid growth of quasi-money deposits which now account for about 80 percent of total liquidity. These deposits are largely denominated in foreign currency and, given the open system, earn internationally competitive rates.

IV. Report on the Discussions

The discussions focused on the recent unfavorable changes in economic circumstances and on the budgetary situation, especially with respect to the public sector wage bill. In addition, reflecting Executive Directors' interest expressed during the 1984 consultation discussions, the land tenure problems and the large share of the budget required for education were examined. Drafting of the Second National Development Plan (1987-91) was not sufficiently advanced for detailed discussions. However, the staff has prepared a medium-term scenario for the balance of payments and external debt as background for assessing development policies.

The Government intends, with the cooperation of the IBRD, to hold an aid donors' conference in mid-1986 to discuss the Second National Development Plan (1987-91).

^{1/} Valuation adjustments on account of exchange rate adjustments have reduced the SDR value of outstanding debt by SDR 1.5 million over the past four years.

Table 2. Vanuatu: Monetary Survey, 1981-85

(In millions of vatu)

	1981	1982	1983	1984				1985		
				March	June	Sept.	Dec.	March	June	
Net foreign assets	<u>2,361</u>	<u>4,081</u>	<u>5,830</u>	<u>7,090</u>	<u>7,685</u>	<u>9,172</u>	<u>9,508</u>	<u>9,754</u>	<u>10,619</u>	
Of which: commercial banks <u>1/</u>	1,589	3,457	5,180	6,463	7,040	8,488	8,692	8,958	9,662	
Domestic credit	<u>1,818</u>	<u>2,371</u>	<u>2,875</u>	<u>2,554</u>	<u>2,432</u>	<u>2,350</u>	<u>2,264</u>	<u>2,462</u>	<u>2,688</u>	
(12-month percentage change)	(13.3)	(30.8)	(21.3)	(10.8)	(-13.8)	(-9.1)	(-21.3)	(-3.6)	(24.1)	
Government (net)	-1,322	-881	-685	-1,267	-1,159	-1,221	-1,264	-1,238	-1,211	
Public enterprises	--	--	68	3	2	2	30	35	85	
Private sector	3,135	3,252	3,492	3,818	3,589	3,569	3,498	3,665	3,814	
(12-month percentage change)	(18.5)	(3.7)	(7.4)	(15.0)	(1.9)	(9.4)	(0.2)	(-4.0)	(6.3)	
Other items (net)	<u>412</u>	<u>554</u>	<u>876</u>	<u>1,351</u>	<u>1,320</u>	<u>1,276</u>	<u>1,194</u>	<u>1,440</u>	<u>1,938</u>	
Total liquidity	<u>3,762</u>	<u>5,898</u>	<u>7,829</u>	<u>8,293</u>	<u>8,797</u>	<u>10,246</u>	<u>10,578</u>	<u>10,776</u>	<u>11,369</u>	
(12-month percentage change)	(-20.0)	(56.8)	(32.7)	(65.6)	(54.0)	(41.0)	(35.1)	(29.9)	(29.2)	
Money	1,266	1,470	1,840	1,719	1,872	1,961	2,134	2,181	2,159	
Quasi-money	2,496	4,428	5,989	6,574	6,925	8,285	8,444	8,595	9,210	
				(In percent per annum, end of period)						
Memorandum items:										
Deposits										
(3 months) <u>2/</u>										
Vatu	8.75-10.75	8.00-10.50	8.00-9.50	8.25-9.25	7.00-9.50	6.50-9.75	6.75-8.75	7.50-8.00	7.00-8.50	
Australian dollar	--	12.50	7.50	11.25	11.63	9.63	10.75	14.00	15.00	
Euro-dollar	--	10.00	10.50	10.75	11.75	11.00	10.38	8.94	7.69	

Source: Central Bank of Vanuatu.

1/ Includes net claims on exempt banks and other offshore financial institutions.2/ Rates quoted in Vanuatu.

Table 3. Vanuatu: Medium-term Projections of the Balance of Payments and Public External Debt, 1985-90

(In millions of SDRs)

	1985 Est.	1986	1987	1988	1989	1990
		Projections				
Trade balance	-33.5	-35.8	-37.0	-40.6	-44.0	-46.6
Export, f.o.b.	17.1	17.7	20.7	21.8	23.3	26.1
Imports, f.o.b.	50.6	53.5	57.7	62.4	67.3	72.7
Of which: for home consumption	47.5	50.3	54.3	58.6	63.3	68.4
Services and transfers (net)	28.1	29.5	28.2	28.5	27.0	26.7
Services (net)	-3.3	-0.8	-0.3	--	-0.1	-0.4
Receipts	41.9	46.1	48.5	50.9	53.0	55.1
Of which: inward travel	17.6	21.0	22.5	24.0	25.7	27.5
Payments	45.2	46.9	48.8	50.9	53.1	55.5
Of which: investment income	10.0	10.3	10.8	-11.3	11.9	12.5
Private transfers (net)	6.5	6.6	6.8	7.0	7.2	7.4
Official transfers (net)	24.9	23.7	21.7	21.5	19.9	19.7
Current account balance	-5.4	-6.3	-8.8	-12.1	-17.0	-19.9
Current account balance exclud- ing official transfers	-30.3	-30.0	-30.5	-33.6	-36.9	-39.6
Nonmonetary capital (net)	11.0	10.9	11.9	12.9	13.9	14.9
Long-term capital	11.0	10.9	11.9	12.9	13.9	14.9
Official	2.8	3.7	4.7	5.7	6.7	7.7
Of which: loan disburse- ments	3.0	4.1	5.2	6.3	7.1	8.2
Private	8.2	7.2	7.2	7.2	7.2	7.2
Short-term capital	--	--	--	--	--	--
Errors and omissions	--	--	--	--	--	--
Overall balance	5.6	4.6	3.1	0.8	-3.1	-5.0
External debt	6.6	10.3	15.0	20.7	27.4	35.1
Debt service	<u>0.71</u>	<u>0.84</u>	<u>1.06</u>	<u>1.23</u>	<u>1.34</u>	<u>1.50</u>
Interest (old debt)	0.21	0.22	0.23	0.24	0.22	0.21
Interest (new debt)	0.08	0.19	0.33	0.50	0.71	0.94
Amortization	0.42	0.43	0.50	0.49	0.41	0.35
Debt service ratio <u>1/</u>	4.0	4.8	5.1	5.6	5.8	5.8

Source: Staff estimates.

1/ With respect to merchandise exports.

Table 4. Vanuatu: Summary of Central Government Fiscal Operations, 1981-85

(In millions of vatu)

	1981	1982	1983	1984		1985	
		Actuals		Budget	Actual	Budget	Estimate
Total revenue and grants	5,303.7	4,957.1	4,493.6	4,963.6	5,759.0	5,539.0	5,412.0
Revenue	1,369.6	1,607.4	1,892.4	2,208.0	2,503.4	2,769.0	2,727.0
Tax	1,019.5	1,264.9	1,467.9	1,796.0	2,037.4	2,308.0	2,202.0
Nontax	350.1	342.5	424.5	412.0	466.0	461.0	525.0
Foreign grants	3,934.1	3,349.7	2,601.2	2,755.6	3,255.6	2,770.0	2,685.0
Recurrent	899.1	743.2	559.4	490.0	436.9	370.0	285.0
Technical assistance	1,635.0	1,497.0	1,050.0	900.0	1,270.0	1,300.0	1,300.0
Development	985.0	1,078.5	991.8	1,000.0	1,041.0	1,100.0	1,100.0
STABEX and other	415.0	31.0	--	365.6	507.7 ^{1/}	--	--
Total expenditure	4,739.4	5,295.4	4,550.3	4,780.7	5,306.2	5,478.0	5,442.0
Recurrent	2,042.6	2,327.0	2,419.1	2,648.8	2,657.9	3,078.0	3,042.0
Of which: wages	(1,170.8)	(1,305.5)	(1,361.8)	(1,627.5)	(1,543.8)	(1,775.0)	(1,749.0)
Technical assistance	1,635.0	1,497.0	1,050.0	900.0	1,270.0	1,300.0	1,300.0
Development	1,046.8	1,071.4	1,081.2	1,000.0	1,068.4	1,100.0	1,100.0
In cash	(504.8)	(423.4)	(536.2)	(...)	(518.4)	(...)	(500.0)
In kind	(542.0)	(648.0)	(545.0)	(...)	(550.0)	(...)	(600.0)
Other ^{2/}	15.0	400.0	--	231.9	309.9	--	--
Overall surplus or deficit (-)	564.3	-338.3	-56.7	182.9	452.8	61.0	-30.0
Financing	-564.3	338.3	56.7	-182.9	-452.8	-61.0	30.0
Foreign (net)	-23.0	-26.0	-21.0	-33.0	-18.7	23.6	23.6
Borrowing	(--)	(--)	(--)	(--)	(8.7)	(55.0)	(55.0)
Repayments	(-23.0)	(-26.0)	(-21.0)	(-33.0)	(-27.4)	(-31.4)	(-31.4)
Domestic (net) ^{3/}	-541.3	364.3	77.7	-149.9	-434.1	-84.6	6.4
Bank ^{4/}	(-768.0)	(435.0)	(189.0)	(...)	(-566.0)	(...)	(...)
Nonbank ^{5/}	(226.7)	(-70.7)	(-111.3)	(...)	(131.9)	(...)	(...)
Memorandum item:							
Overall deficit (-)							
excluding foreign grants	-3,369.8	-3,688.0	-2,657.9	-2,572.7	-2,802.8	-2,709.0	-2,715.0

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

^{1/} Comprises grants received from STABEX, however, the 1984 outcome includes VT 142 million U.K. grant to the civil disturbance claims fund.

^{2/} Comprises transfer of funds received from STABEX to the Vanuatu Commodities Marketing Board.

^{3/} Residual.

^{4/} Changes in net claims on the Government as defined in the monetary survey tables.

^{5/} Estimated as a residual. Includes contra-entry for changes in net deposits of certain special funds, sundry net creditors, and adjustment for timing differences.

APPENDIX I

- 19 -

Vanuatu

Basic Data

Area:	12,000 square kilometers			
Population:	130,000			
Population growth:	3.0 percent			
GDP per capita (1984):	SDR 730			
	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985 1/</u>
Output and price (annual rate of change in percent)				
Real GDP	2.0	3.0	5.0	-3.0
Consumer prices	6.2	1.7	5.5	3.0-4.0
Money and credit (annual rate of change in percent)				
Broad money	56.8	32.7	35.1	29.2 <u>2/</u>
Total domestic credit	30.8	21.3	-21.3	10.5 <u>2/</u>
Credit to private sector	3.7	7.4	0.2	6.3 <u>2/</u>
Credit to government (net)	33.4	22.3	-84.5	4.5 <u>2/</u>
Public finance (annual rate of change in percent)				
Total revenue and grants	-6.5	-9.4	28.2	-6.0
Foreign grants	-14.9	-22.2	25.2	-17.5
Of which: recurrent budget	-17.3	-24.8	-21.9	-34.8
Total expenditure	11.7	-14.1	16.6	2.6
Current expenditure	13.9	4.0	9.9	14.5
Balance of payments (SDR millions)				
Exports (f.o.b.)	9.7	16.8	30.8	17.1
Imports (f.o.b.)	39.6	42.6	50.0	50.6
Trade balance	-29.9	-25.8	-19.2	-33.5
Current account balance <u>3/</u>	9.9	3.2	19.0	-5.4
Overall balance <u>4/</u>	16.2	16.5	39.6	5.6
Terms of trade (percent change)	-18.6	33.7	55.9	-47.8
	(Annual percent change)			
Gross official reserves (end of period)				
In millions of SDRs	12.4	10.2	15.2	16.2
In months of imports	3.8	2.8	3.6	4.0
Exchange rates				
Vatu/SDR <u>5/</u>	106.2	106.2	100.6	110.0 <u>6/</u>
Nominal effective exchange rate <u>7/</u>	90.0	92.5	102.6	103.2 <u>6/</u>
Real effective exchange rate <u>7/</u>	98.3	99.5	109.4	111.0 <u>6/</u>
Selected financial ratios (in percent)				
Current account/GDP	13.4	4.1	20.5	-6.4
Government budget deficit/GDP	-4.2	-0.7	4.9	-0.3
External debt/GDP	4.9	4.4	4.2	7.9 <u>8/</u>
External debt service ratio <u>9/</u>	5.2	3.0	1.9	4.1 <u>8/</u>
Foreign grants/GDP <u>10/</u>	41.8	31.0	35.0	28.8

1/ Staff estimates.2/ Twelve months ending June.3/ Including official transfers.4/ Based on the net foreign asset position of the monetary system.5/ End of period.6/ June 1985.7/ Fourth quarter average. Trade-weighted 1980=100.8/ Increases in ratios mainly reflect effects of the January 1985 cyclones on GDP and exports.9/ Percent of exports of goods.10/ Foreign grants inclusive of capital and technical assistance grants.

Vanuatu: Relations with the Fund
(As of September 30, 1985)

I. Membership status

- (a) Date of membership: September 28, 1981
(b) Status: Article VIII

A. Financial Relations

II. General Department
(General Resources Account)

- (a) Quota: SDR 9.0 million
(b) Total Fund holdings of currency: SDR 7.419 million
(82.4 percent of quota)
(c) Fund credit: None
Of which: Credit tranches: None
Special facilities: None
(d) Reserve tranche position: SDR 1.581 million
(17.6 percent of quota)
(e) Current operational budget: None
(f) Lending to the Fund: None

III. Stand-by or extended arrangement
and special facilities

- (a) Stand-by or extended arrangement: None
(b) Special facilities: None

Vanuatu has not used Fund resources since becoming a member in 1981.

IV. SDR Department

- (a) Net cumulative allocation: None
(b) Holdings: SDR 132,317
(c) Current Designation Plan: None

V. Administered Accounts

- (a) Trust Fund loans:
(i) Disbursed: None
(ii) Outstanding: None
(b) SFF Subsidy Account: None

VI. Overdue obligations to the Fund: None