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December 27, 1993

To: Members of the Executive Board

From: The Secretary

Subject: Luxembourg - Staff Report for the 1993 Article IV Consultation

Attached for consideration by the Executive Directors is the staff report for the 1993 Article IV consultation with Luxembourg, which is tentatively scheduled for discussion on Monday, January 24, 1994.

Mr. Öberg (ext. 36629) or Mr. Halikias (ext. 38972) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

Unless the Documents Preparation Section (ext. 36760) is otherwise notified, the document will be transmitted, in accordance with the procedures approved by the Executive Board and with the appropriate deletions, to the Commission of the European Communities (CEC), the GATT Secretariat, and the Organisation for Economic Cooperation and Development (OECD), following its consideration by the Executive Board.

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INTERNATIONAL MONETARY FUND

LUXEMBOURG

Staff Report for the 1993 Article IV Consultation

Prepared by the Staff Representatives for the
1993 Consultation with Luxembourg

Approved by Michael C. Deppler and Mark Allen

December 23, 1993

I. Introduction

Article IV consultation discussions were held in Luxembourg during October 20-26, 1993. 1/ The staff team consisted of S. Öberg (Head), C. Bismut, I. Halikias, and F. Lakwijk (all EU1). Mr. de Groote, Executive Director, attended the concluding session and Mr. Heinen, Assistant to the Executive Director, most of the meetings. The mission met with the Prime Minister, the Minister of Finance, the Director-General of the Luxembourg Monetary Institute, and other officials.

At the previous consultation, 2/ Executive Directors commended the authorities for the successful design and implementation of their economic policies and encouraged them to maintain a medium-term policy orientation. However, they also pointed to risks in the short-term of overheating from the tightness of the labor and real estate markets and expressed concern about the rapid expansion of claims on the social product, in particular in the area of social security. Directors also encouraged the authorities to raise official development assistance further.

II. Background

1. Long-term economic performance

Luxembourg's economic performance since the early 1980s has been stronger than in most other European countries. From 1982 to 1992, economic growth in Luxembourg averaged about 4 percent a year and unemployment

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1/ The 1993 discussions had been scheduled to take place earlier, but were postponed owing to the preference of the authorities for a mission in October; a notification of delay has been issued to the Executive Board on December 1, 1993 (EBD/93/179).

2/ The consultation was concluded at the Board on December 16, 1991 (EBM/91/169). The Chairman's summing-up was circulated as SUR/91/110.

remained within the range of 1 to 2 percent. Inflation was lower than the EU average but slightly higher than in neighboring countries, and the external current account surplus averaged over 15 percent of GDP (Chart 1).

While the strong long-term performance can partly be attributed to favorable endowments such as a central geographical location, a multilingual labor force, and social and political stability, it also owed much to economic management. Active industrial policies and accommodative changes to the legislative and tax environment supported the rapid change from high dependence on the steel industry, which was faced with a fall-off in demand in the mid-1970s, to a more diversified and less vulnerable production structure. An active diversification policy helped non-steel manufacturing increase its share in GDP. Even more impressive is the rapid growth of the financial sector. A strict bank secrecy code, liberal laws and regulations, and generous tax provisions encouraged the transformation of Luxembourg into a major financial center. More recently, the swift adoption of EC directives concerning collective investment funds has made it possible for the banking sector to move quickly and successfully into the area of mutual and pension fund management.

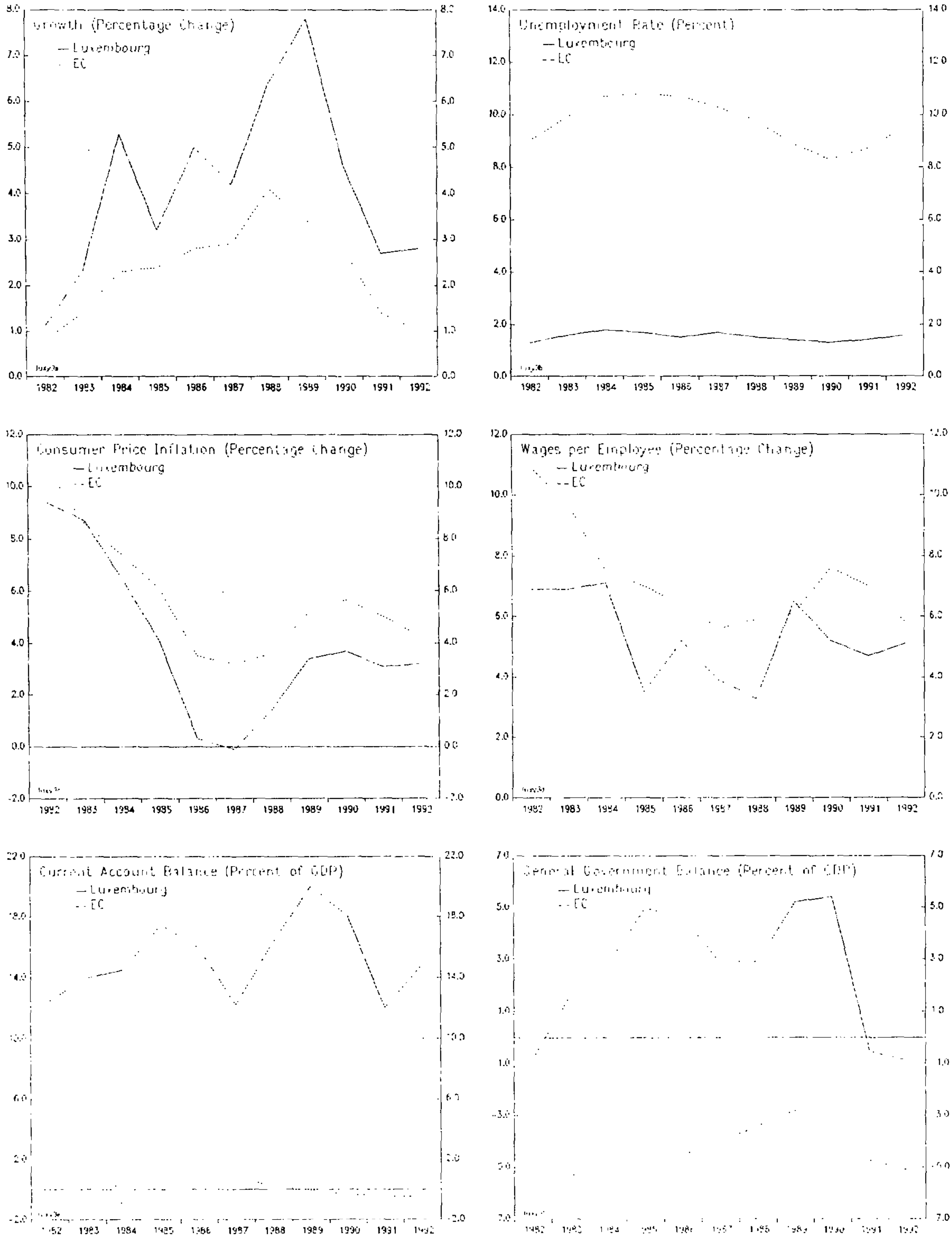
Sound public finances in the 1980s also enhanced the economy's performance. Public expenditure growth was strong, particularly in the second half of the decade. Total public expenditures increased by more than 6 percent a year in real terms from 1985 to 1990, and social spending by more than 7 percent a year, in spite of increasing real wages and low unemployment. Even higher real growth rates were registered for important parts of social security such as pensions (nearly 9 percent) and health (nearly 10 percent). But GDP growth was also strong, resulting in rapidly increasing revenues, repeated budget surpluses, and the virtual disappearance of net government debt (Chart 2).

2. Recent economic developments

More recent economic performance has been weaker, but still compares favorably to that of most other European countries. Growth has slowed down as neighboring countries have entered recession, but is still expected to be about 2 percent in both 1993 and 1994, as domestic demand continues to expand and service sector growth remains relatively buoyant. Unemployment has grown, but is still very low. Wage increases, however, have been higher than in neighboring countries. At the same time, inflation has been rising, as increases in indirect taxes, public tariffs, and medical care prices more than offset the impact of moderate import price rises. The current account surplus remains very large, with a surplus on the service account more than compensating for the trade deficit.

CHART 1
LUXEMBOURG

Long-Term Economic Performance

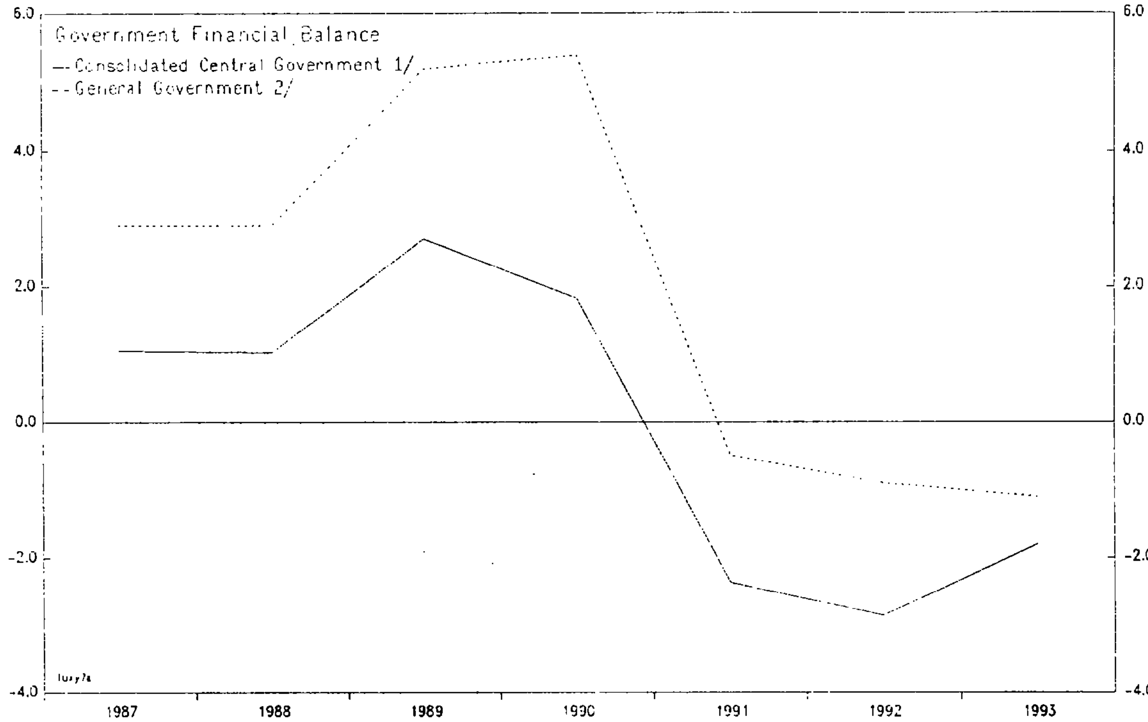


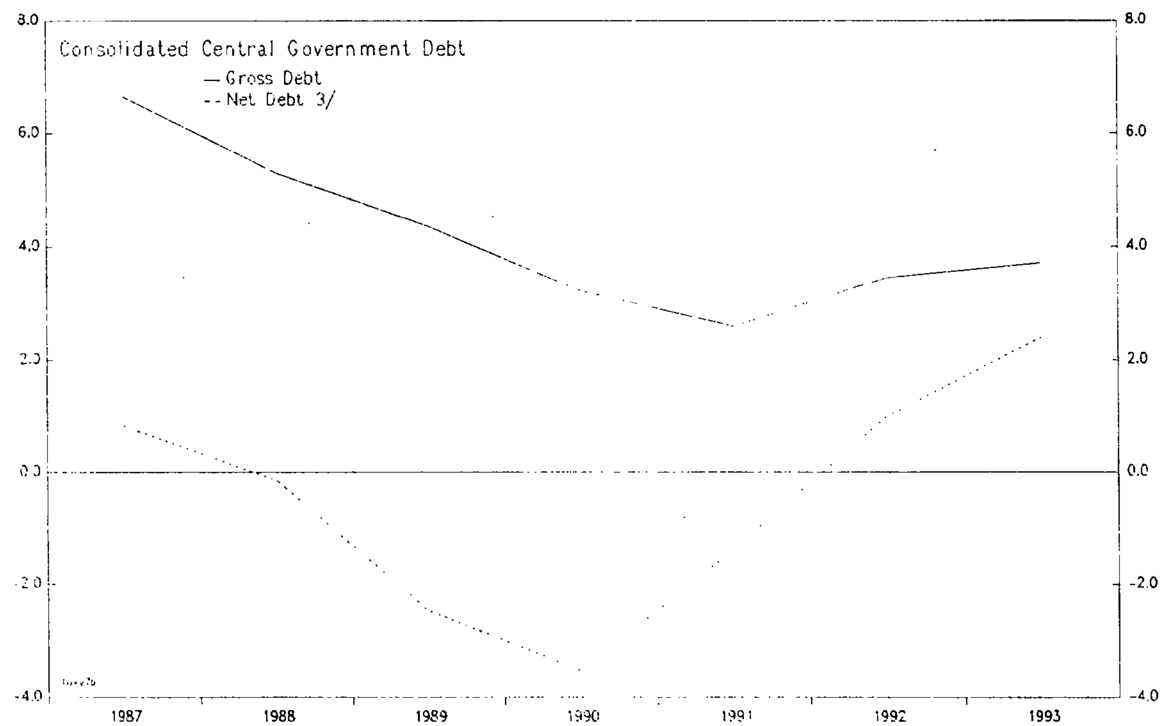
Sources: EC, European Economy; Eurostat, Eurostatistics; STATEC; [illegible]

CHART 2
LUXEMBOURG

Public Finances

(Percent of GDP)





Sources: Budget documents; and data provided by the authorities.
1/ Including special state funds.
2/ Not including local government.
3/ Gross debt minus budgetary reserves and reserves of the state investment funds.

Recent Economic Developments

	1991	1992	Est. 1993
Gross domestic product (percentage change)	2.7	2.8	2.0
Unemployment (percent of labor force)	1.4	1.6	2.0
Consumer prices (percentage change)	3.1	3.2	3.8
Current account (percent of GDP)	12.0	14.8	...

Fiscal performance has also been weaker in recent years. The central government budget balance (including social security) has turned into a small deficit since 1991. Two main reasons underlay this deterioration. First and most important, expenditure growth was particularly strong from 1989 to 1991, resulting in a significant increase in the share of public expenditures in GDP. Second, there was a substantial cut in direct taxes in 1991, which more than outweighed the revenue impact of an increase in the normal VAT rate in 1992 prompted by EC tax harmonization efforts. Although the revenue to GDP ratio has declined somewhat, it is still above the EC average, mainly reflecting unusually large revenue from corporate income taxes and property taxes.

Central Government and Social Security

(In percent of GDP)

	1989	1990	1991	1992	Est. 1993
Revenue	46.5	47.4	45.4	45.0	44.6
Expenditures	41.3	42.0	45.9	45.9	45.7
Balance	5.2	5.4	-0.5	-0.9	-1.1

On the monetary front, there was a gradual improvement of conditions until the summer of 1993. Monetary and exchange rate policies are managed within the framework of Luxembourg's monetary association with Belgium, 1/ and the association's policy of closely following the D-mark gained credibility over the 1980s and early 1990s. Short-term interest rate differentials with Germany disappeared and the yields on Belgian government bonds gradually approached those on German bonds (Chart 3). The franc was stable relative to the D-mark, with variations only within a very narrow band, between May 1990, when the Belgian authorities announced that the franc would closely track the strongest currency within the ERM (the "franc fort" policy), and August 1993 (Chart 4).

However, the Belgian franc came under pressure during 1993. Belgian short-term interest rates had to be raised temporarily in the spring and more substantially at the end of July. Between the widening of the ERM bands in early August and the time of the mission in late October, the Belgian and Luxembourg francs depreciated by more than 5 percent against the D-mark, in spite of an increase in the short-term interest rate differential by about 3 percentage points and continued interventions in the currency markets by the Belgian central bank. The long-term interest rate differential also increased to more than 1 percent, after having decreased until July (Chart 5).

Moreover, a significant negative differential between Luxembourg and Belgian bond yields reemerged, possibly indicating renewed market expectations of a change in the parity between the two currencies over the long term; the difference had practically disappeared in the fall of 1992 suggesting strengthened credibility of the Belgian franc which was practically unaffected by the crisis in European currency markets at that time (see Chart 3). While the first auction of Luxembourg 10-year linear government bonds in October also resulted in a yield which was significantly below Belgian bonds (96 basis points), the large range of offered prices indicated great uncertainty about the proper interest rate.

Since the time of the mission, the Belgian franc has strengthened again. The Belgian government has announced and obtained approval of the two houses of parliament for a plan aimed at improving public finances and promote employment. The plan has been well received in the financial markets. The Belgian franc has strengthened against other EMS currencies and has returned well within the former narrow (2.25 percent) margins around the central parity in mid-December. The short-term interest differential

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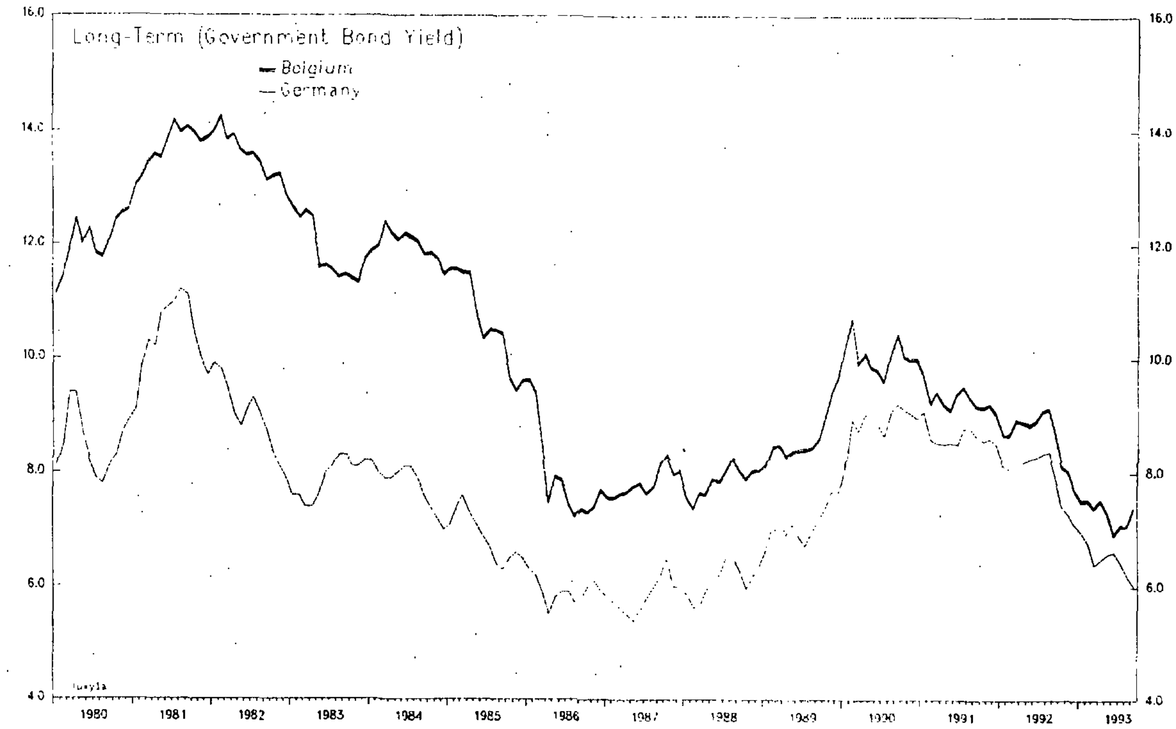
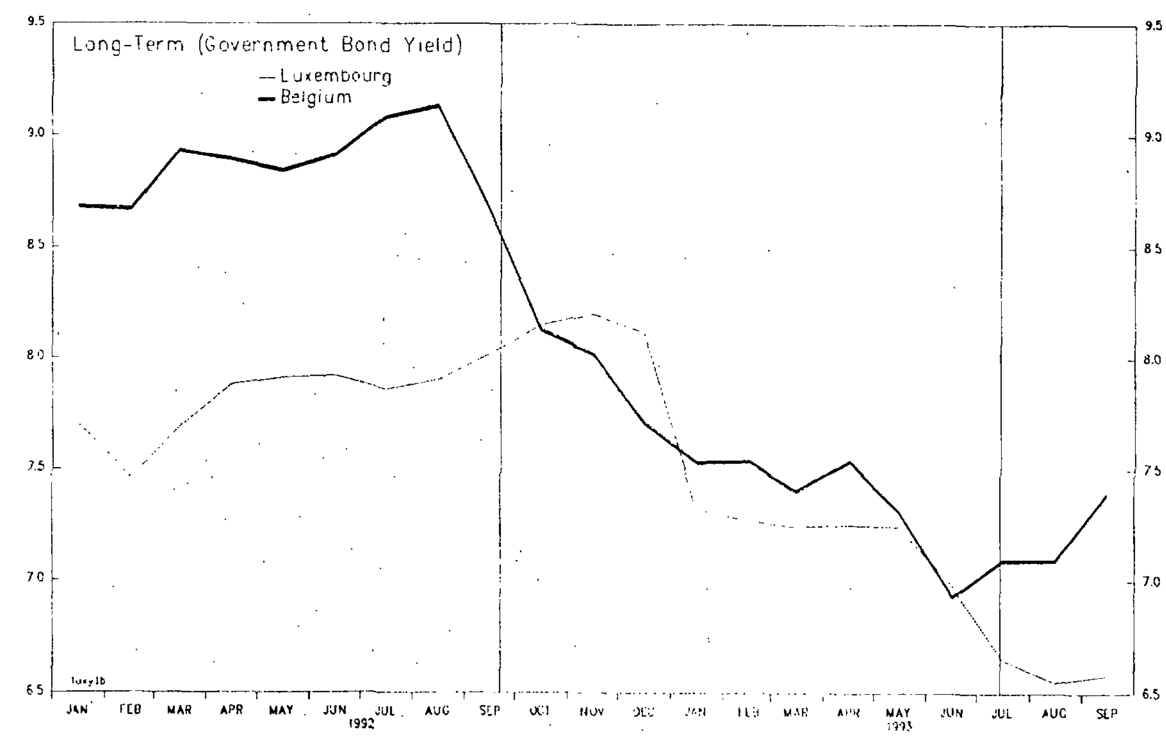
1/ The monetary association between Belgium and Luxembourg was established in 1922, and last year extended until the year 2002 (EMU would, however, if it takes effect before then, supersede the bilateral agreement). Since 1979 both countries are members of the ERM. Their two currencies are at a par, and the Belgian franc is legal tender in Luxembourg. The Belgian National Bank is responsible for executing monetary policy, and the Luxembourg Monetary Institute (IML) issues notes and coins within certain limits. Shortly after the start of the second stage of the EMU in January 1994, the IML will assume central bank status.

CHART 3
LUXEMBOURG

Interest Rates
(Percent)



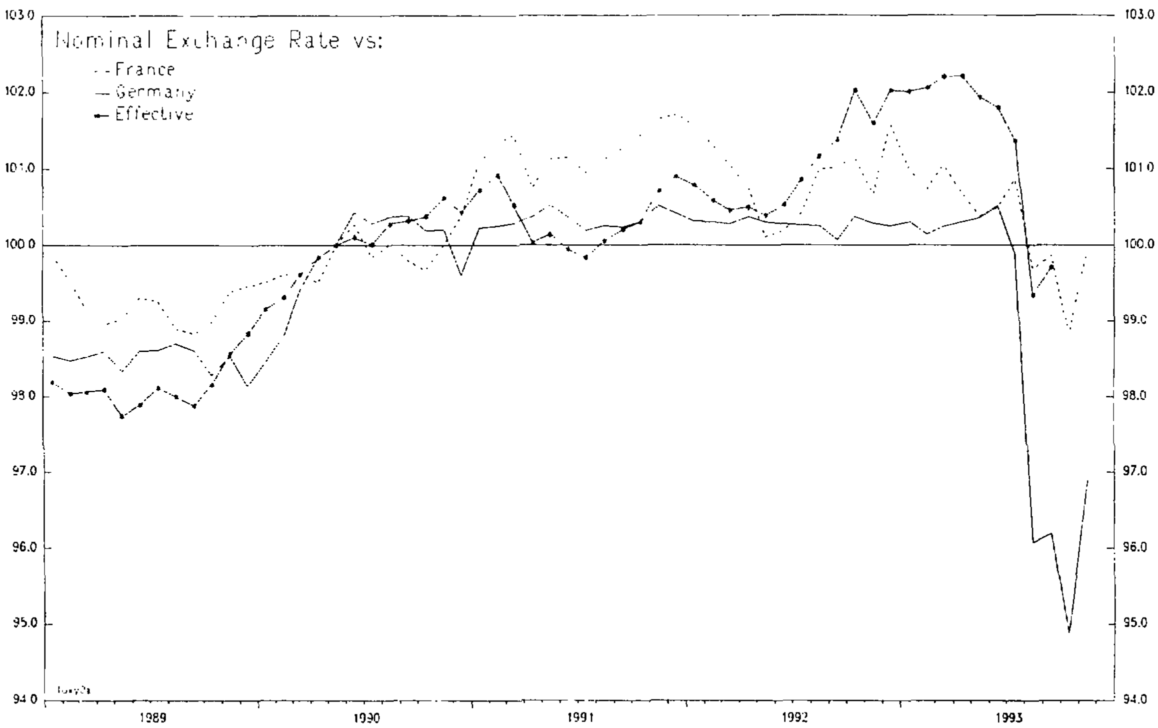


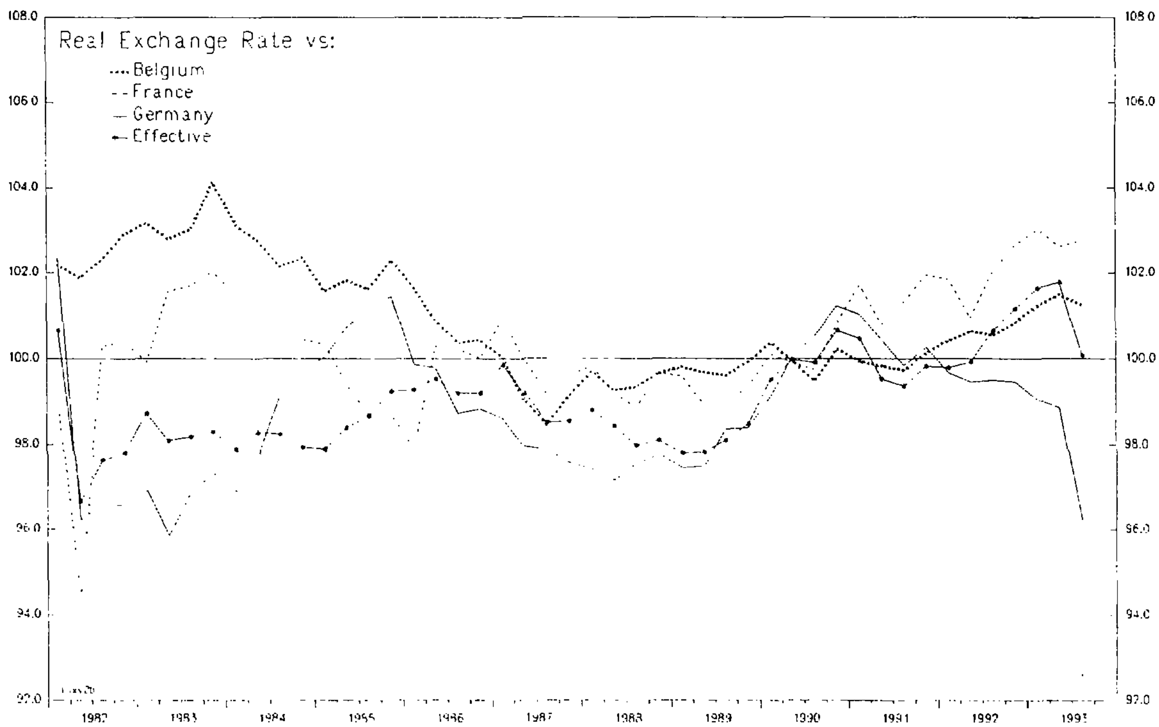
Source: IMF, International Financial Statistics and Eurostat, Eurostatistics

CHART 4
LUXEMBOURG

Exchange Rates

(May 1990=100)





Source: IMF, International Financial Statistics.

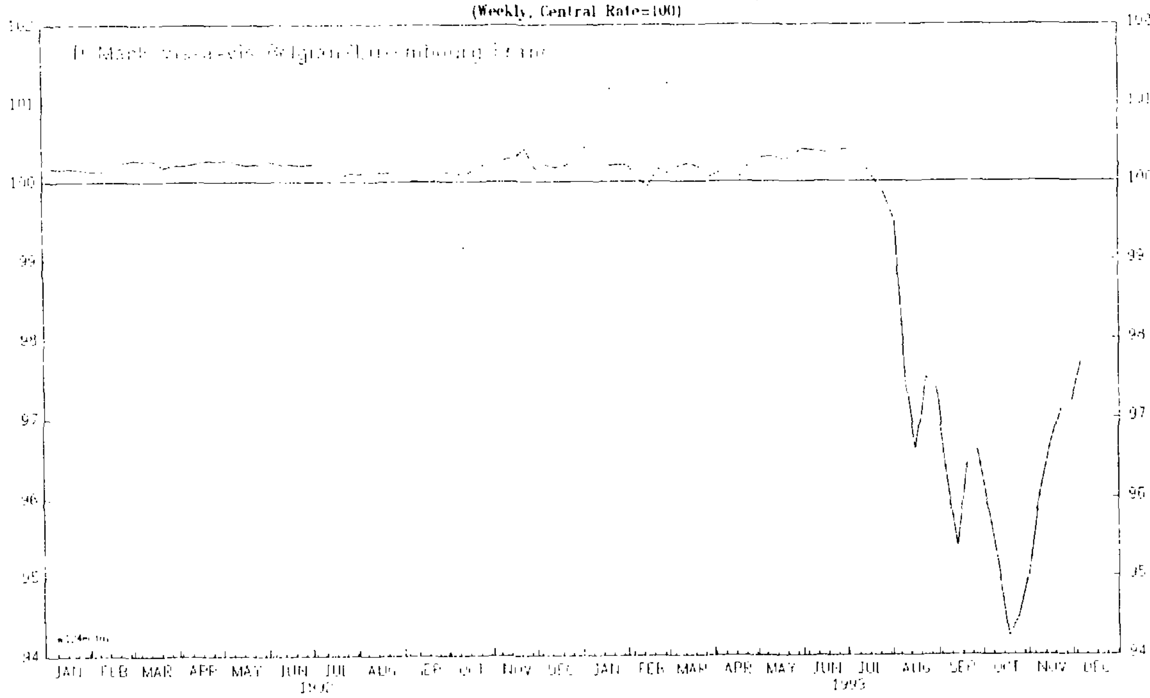
CHART 5

LUXEMBOURG

Exchange Rates and Interest Rates

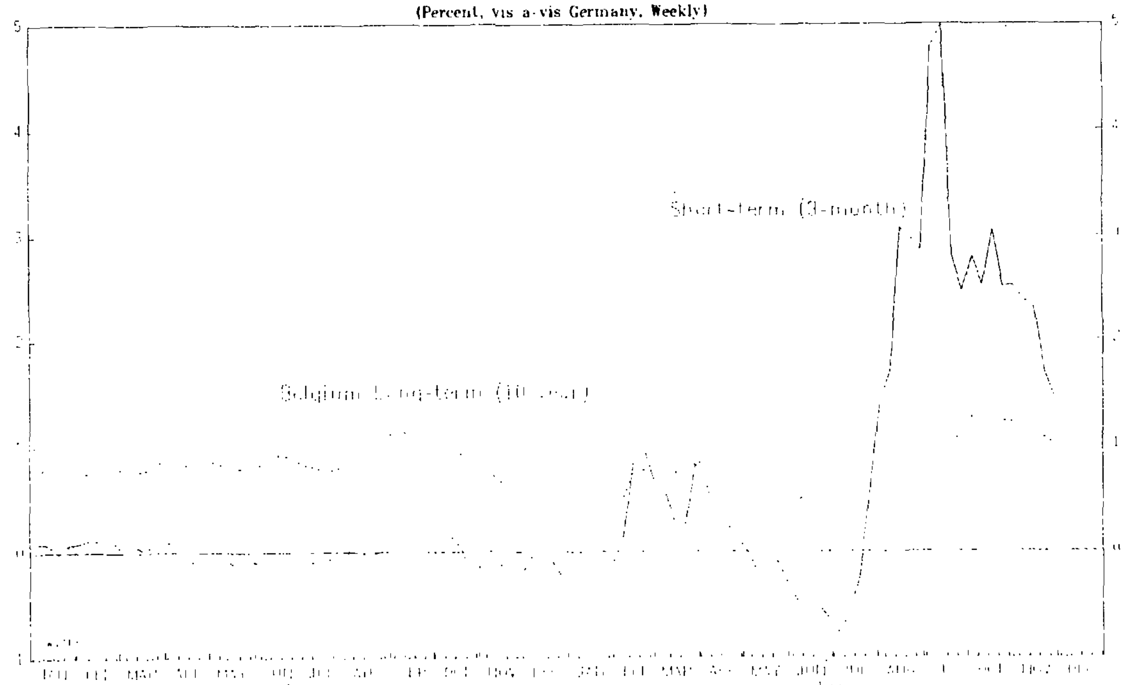
Exchange Rates

(Weekly, Central Rate=100)



Interest Rate Differentials

(Percent, vis a-vis Germany, Weekly)



Source: IMF, Research Department

vis-à-vis Germany has been reduced to a little more than 1 percent, and the long-term interest differential to less than 1 percent.

3. Medium-term prospects

Economic growth over the next few years could fall substantially short of the very high rates observed in the second half of the 1980s. The steel industry is still faced with problems, and other industrial sectors are not likely to expand enough to make manufacturing a significant contributor to growth. Increasing European integration and competition from other financial centers have eroded some of the previous advantages of the financial sector, while prospects for other parts of the services sector are uncertain: for example, further indirect tax harmonization could negatively affect retail trade. Concerns about a continued expansion in the size of the foreign labor force could also limit growth prospects; it already accounts for more than half the total labor force.

Staff calculations indicate that continued strong growth in public expenditures in combination with slower GDP growth would result in large deficits in public finances. Two medium-term scenarios are analyzed to illustrate the relation between economic growth and the evolution of public finances. 1/ They both assume a continuation of the trend growth in real public expenditures (about 6 percent a year from 1985 to 1992) and a fixed revenue to GDP ratio. While real expenditure growth was particularly high from 1989 to 1991 and seems to have declined in 1992 and 1993, the trend in the second half of the 1980s was also strong and the rapid growth in social spending has shown little sign of abating. Pension and health expenditures increased by nearly 6 percent in real terms in 1992 and nearly 8 percent in 1993. The first scenario assumes a GDP growth rate similar to that from 1990 to 1994 (2.4 percent a year) and the other a growth rate similar to that from 1985 to 1990 (5.6 percent a year). The results imply that a sharp decline in public expenditure growth, or a marked rise in the revenue to GDP ratio, would be necessary in order to avoid large deficits in the likely case of relatively modest GDP growth in coming years.

III. Report on Policy Discussions

The discussions concentrated on budgetary policies and future monetary relations with Belgium. Trade policy and assistance to developing countries were also discussed.

1. Budgetary policies

The staff noted that public expenditures had increased very fast, in particular in the social area, and pointed out the risks for large fiscal

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1/ The medium-term scenarios are summarized in Chart 6 and presented in more detail in the recent economic developments paper.

deficits in the medium term if expenditure trends continued. The authorities recognized these risks. They reaffirmed their intentions to keep the deficit small and to limit expenditure growth to below medium-term GDP growth. They had reduced the budget norm from 3.5-4 percent in 1990-1993 to 1.5 percent in 1994. 1/ Significant efforts had been made to control expenditures, but many rigidities remained in the budget process. In addition, the substantial reduction in direct taxes in 1991 had been a main source of fiscal deterioration.

However, the authorities also pointed out that the EC Commission had recognized that Luxembourg was one of the few EC countries with room for manoeuvre in the sphere of fiscal policy. While admitting that the strong public finances of the past had made it easier for Luxembourg than for many other countries to support domestic demand in recent years, the mission expressed the view, in light of the above considerations, that the scope for expansionary fiscal policy was limited. Moreover, fiscal policy was rather ineffective as a short-term policy instrument for supporting domestic activity and reducing further the already low level of unemployment, as Luxembourg was a very small and open economy with a very elastic labor supply.

Moving to the specific areas of expenditure buoyancy, the discussions focused first on problems concerning developments in the pension system. The mission noted that pension expenditures had been growing rapidly in real terms and as a share of GDP (Chart 7). The authorities recognized that the 1991 pension reform had added to future pension liabilities. The pension reform was linked mainly to the restructuring of the steel industry and included improvements in pension benefits and a reduction of the retirement age from 60 to 57 years for people who had worked 33 years or more; civil servants were not covered by this pension system, but by a public pay-as-you-go system without reserves. Despite the reform, the large surplus in the pension system remained nearly unchanged and the reserves equalled 2.5 years of annual expenditures at the end of 1992. However, projections based on present financing and benefit rules showed reserves possibly disappearing early in the next century. This would imply significant increases in contribution rates or reductions in benefits. The authorities recognized the need to raise the retirement age, and suggested that it could be raised to 65 or 67 years, particularly given the shortage of labor.

The mission pointed out that the projections for the pension system would be troublesome for any country, but in the case of Luxembourg there were additional considerations presented by the substantial share of foreign beneficiaries in the total number of pensioners. Retired foreign workers would in many cases be taxed in other countries and would spend a much

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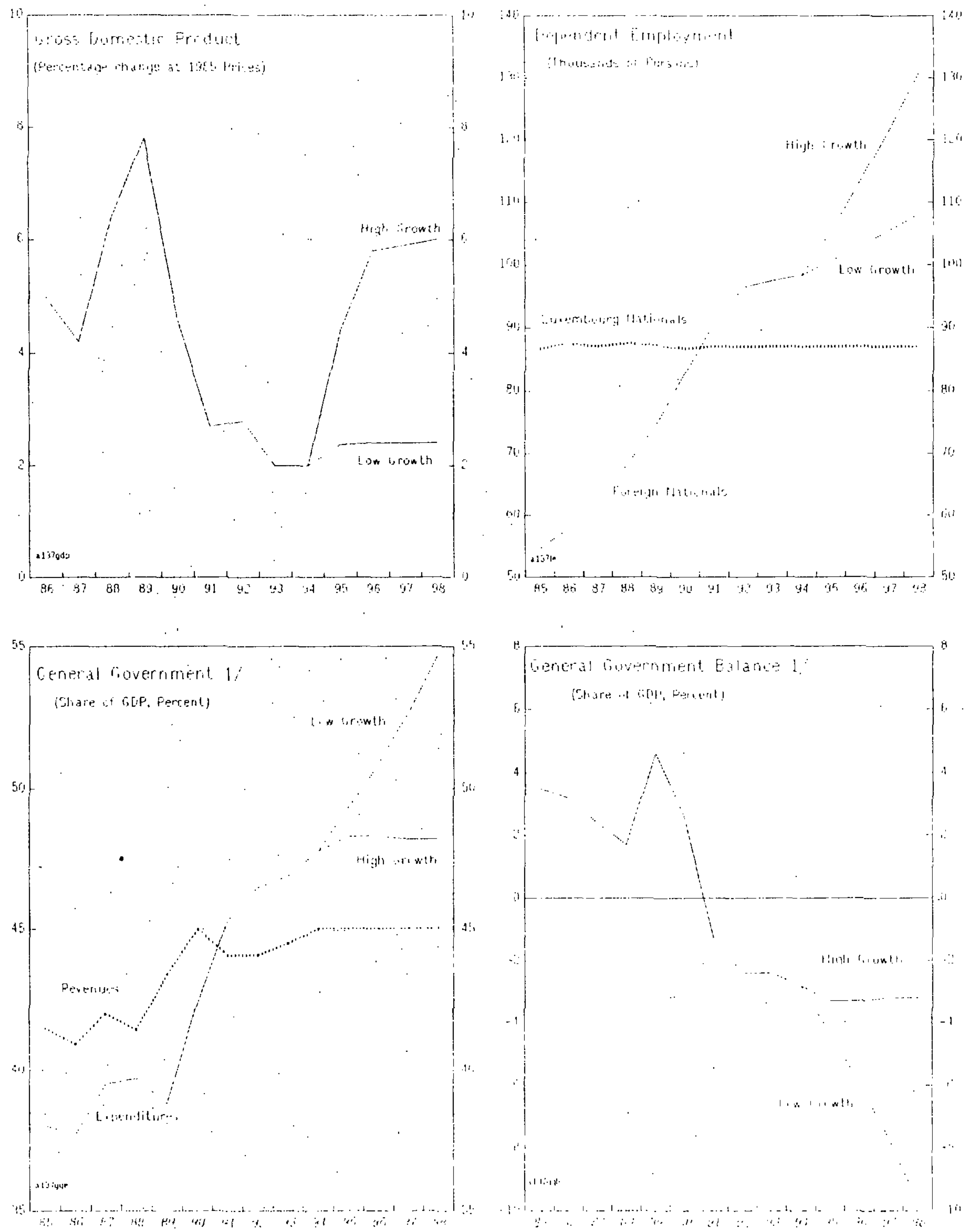
1/ The budget norm is supposed to mirror medium-term growth prospects and determines, together with an assumption about the expected price increase, the ceiling for the budgeted central government expenditures in nominal terms. The budget norm does not, however, include social security.

CHART 6
LUXEMBOURG

Medium-Term Scenarios



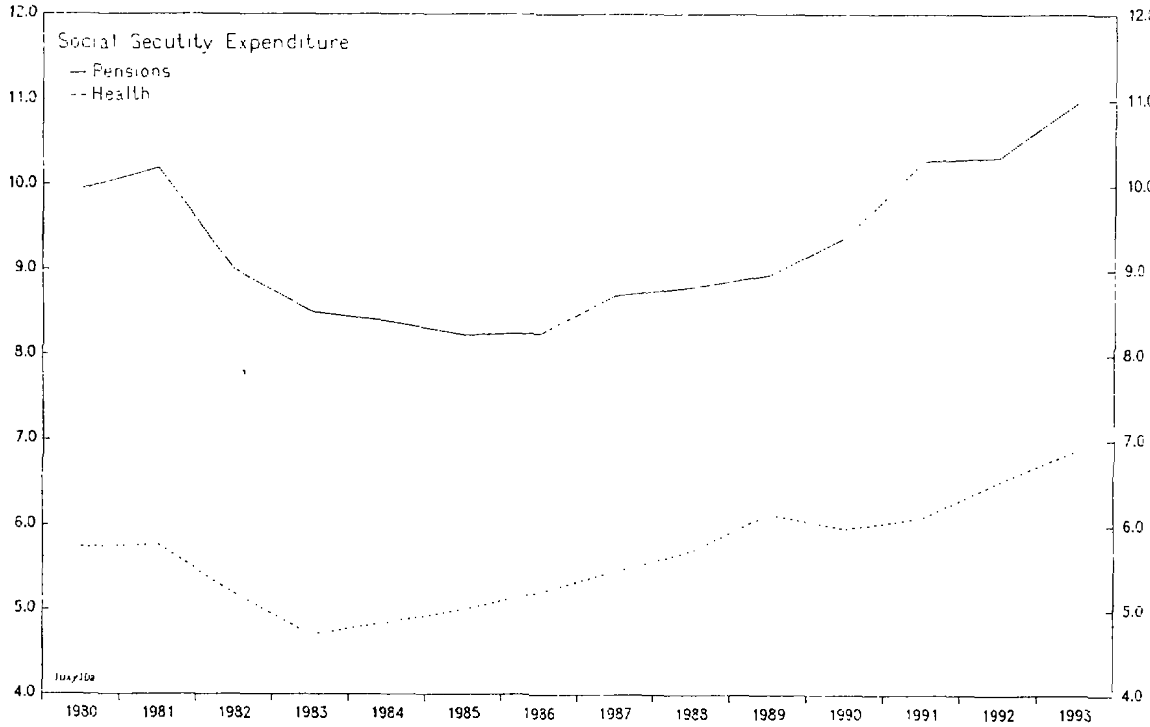
Sources: IMF, Government Finance Statistics; data provided by the authorities; and staff calculations.
1/ Central government and social security.

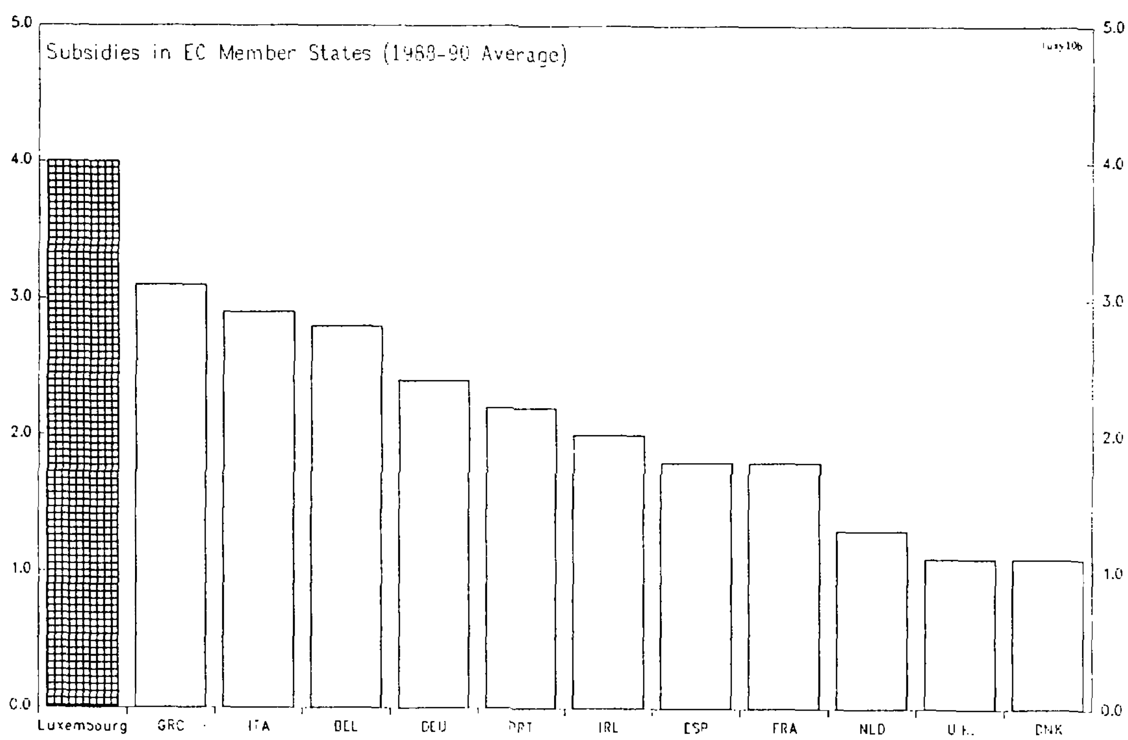
CHART 7

LUXEMBOURG

Social Security and Subsidies

(In Percent of GDP)





Source: IGSS, Rapport général sur la Sécurité Sociale; data provided by the authorities; EC Commission, "Third Survey on State Aid in the European Community", 1992

smaller fraction of their pension income in Luxembourg than residents, thereby reducing the economic and tax benefits to Luxembourg of pension transfers. The problem could be particularly difficult if production conditions deteriorated, leading to a sharp decline in the size of the foreign labor force, as the ratio of total recipients to total contributors would fall significantly. The burden on the national labor force of financing the pensions could increase substantially. The need was thus particularly large in Luxembourg for the pension fund to build up and invest reserves to cover future pension liabilities.

As regards health care, the mission noted that also in this area expenditures had been growing rapidly in real terms and as a share of GDP (see Chart 7). The authorities explained that they had recently introduced a ceiling for the Government's contribution to health insurance of 39 percent of total revenues of the health care system. Furthermore, changes were under way to better control expenditures. Nevertheless, they expected that the private sector contribution rates would have to be increased in 1994. They noted that social security contributions were low relative to neighboring countries, but agreed that increases would have an adverse impact on competitiveness and would be contrary to an EC Commission recommendation to keep social contributions low.

The mission noted that the level of state aid to industry was among the highest in the EC and pointed to the risk for misallocation of resources. 1/ The authorities explained that, due to EC regulations, Luxembourg had to change its legislation in this area recently. The new law only allowed state aid to certain regions (mainly those affected by the decline in the steel industry) and to support to small- and medium-sized enterprises, industrial research and development, and environmental protection and efficient use of energy. Information was not, however, available of the extent to which the new law would reduce total state aid.

2. Monetary and exchange rate arrangements

The recent turbulence in currency markets had generated a public discussion on the monetary and exchange rate arrangements. The debate had focused on two main options. The first was continuing with the current arrangement, and the second abandoning the monetary association with Belgium and linking the Luxembourg franc to the D-mark. The latter would tie Luxembourg to a large and presumably stable currency area with low inflation over the medium term, and with a share in Luxembourg's trade about the same as that of Belgium (the trade share for Belgium was 28 percent and for Germany 30 percent in 1991). This dilemma had not existed as long as the Belgian franc had been linked to the deutsche mark within the narrow band of

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1/ A 1992 study by the EC Commission, "Third Survey on State Aids in the European Community", estimates the overall state aid in Luxembourg at 4.0 percent of GDP in both 1986-1988 and 1988-1990. In the latter period the level was the highest among EC countries (see Chart 7).

the ERM. The enlargement of the band in early August, and the subsequent depreciation of the franc, had raised doubts in financial markets and the public at large about the feasibility of the strong currency option in the future. With this debate in the background, the mission inquired about the authorities views on the issue.

The authorities explained that the monetary association is part of the more general treaty of the Belgian-Luxembourg Economic Union, that the treaty cannot be terminated or amended unless both parties agree, and that only a number of minor modifications in the text of the treaty had been mutually decided on in the past. They also explained that new changes will take place in early 1994 when the Luxembourg Monetary Institute (IML) assumes central bank status. A new law defining the monetary status of the IML had just been approved by the Council of Ministers. The law specified price stability as the goal of monetary policy, stipulated central bank independence, and provided the IML with the full range of policy instruments that are included in the Maastricht treaty text.

The authorities remarked that they were not overly worried about the limited depreciation of the Belgian franc and the related increase in interest rates. They noted that the depreciation should be seen in perspective (the D-mark had appreciated by around 50 percent against the franc since the early 1970s), and that the franc had actually appreciated by about 2 percent in nominal and real effective terms since before the currency crisis started. Moreover, the increase in interest rates would not have significant negative effects on capital formation, as investment decisions in Luxembourg depended mostly on strategic decisions by the investing companies and were little affected by domestic short-term interest rates. Finally, the impact on inflation of any further substantial depreciation of the franc could be contained, if needed, by a suspension of the wage indexation mechanism. 1/

The authorities also emphasized that a separation of the two currencies would involve breaking the treaty with Belgium, which they had no intention of doing and which would have negative repercussions that extended beyond the monetary sphere. The political costs would be large. There would also be practical and other problems linked to a break-up of the association. The difficulties of implementing a new monetary policy regime would be considerable, even though the new legislation for the IML would make it less of a problem than hitherto. Moreover, a distinction would have to be made between, for example, assets denominated in Belgian and Luxembourg francs, and while some distinction already existed between different types of deposits, the separation would create confusion in other areas. Finally,

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1/ All wage contracts include by law an index clause which automatically raises wages when consumer prices have increased by more than 2.5 percent since the last index-linked wage adjustment; the wage indexation is viewed by the authorities as contributing to stability in Luxembourg without having significant negative effects on competitiveness.

there could be costs to obtaining a bilateral agreement needed for linking the currency to the D-mark.

Against this, the authorities noted that the benefits of abandoning the monetary association with Belgium and linking to the D-mark were uncertain. With credibility in the Belgian franc restored, Luxembourg would not gain much by linking directly to the D-mark instead of indirectly through the Belgian franc. In addition, if the third stage of EMU were to take effect within a few years, most of the possible gains of a change would apply only to a relatively short period.

In conclusion, given the limited depreciation of the Belgian franc, the authorities saw no reason to abandon the longstanding monetary association with Belgium. In the long run, however, Luxembourg would prefer to be member of a larger European economic and monetary union and was going to concentrate on fulfilling the Maastricht criteria to be able to join the third stage of EMU when it started.

3. Trade policy and assistance to developing countries

On the GATT negotiations, the authorities expressed in general a desire to reach agreement, but also some reservations. They noted that, as a small country in the center of Europe, Luxembourg had benefitted greatly from international integration. However, they were not fully satisfied with the Blair House agreement, because it did not remove certain specific disadvantages for Luxembourg farmers. Furthermore, Luxembourg favored the opening of markets to imports of steel from Eastern Europe, but only if it occurred in an orderly fashion; the EC had entered into formal agreements to this end with the Czech and Slovak Republics and with Poland.

The mission encouraged the authorities to support a successful conclusion of the Uruguay Round. As a result of its high international orientation Luxembourg was likely to benefit from such an agreement. Even if an agreement could have some short run negative effects on sectors like steel and agriculture, these effects would probably be limited. In the steel sector, restructuring was more advanced in Luxembourg than in many other countries.

On official development assistance (ODA), the mission noted that, despite the wealth of the country, Luxembourg's share of ODA in GDP was low (0.3 percent in 1993). The mission encouraged the authorities to increase the assistance to developing countries and to contribute to the financing of the ESAF successor. The authorities referred to the large increase of ODA between 1990 and 1993 and expressed their intention to raise ODA to 0.35 percent of GDP by 1995 and to 0.7 percent of GDP by the year 2000.

IV. Staff Appraisal

Luxembourg is still doing well economically compared to most other European countries, but also faces potential problems. The most important is the continued strong growth of public expenditures. If current trends for public expenditures were to continue, both public finances and the economy as a whole would be adversely affected (except if economic growth turned out to be similar to that in the late 1980s, a situation which should not be counted on). In particular, the raising of taxes and/or the emergence of larger deficits in public finances would be inevitable. Given the desirability of holding down the overall tax burden and avoiding public sector deficits, total public expenditures, and in particular social spending, should not be allowed to grow as fast as they have been doing in the past. The staff thus welcomes the Government's decision to lower the budget norm in the 1994 budget. A medium-term orientation of fiscal policies and the maintenance of strong budgets has served Luxembourg well in the past and should continue, and the authorities are encouraged to return to a situation with a balanced central government budget.

Attention needs to focus in the first instance on the pension system. Despite its seemingly high current level of reserves, it is out of balance over the longer run. In correcting this, changes ought to be made to reach a better balance between present contributions and future liabilities. In particular, consideration should be given to raising the retirement age, similar to changes underway or under discussion in other countries, to relieve future pressures on both private and public pension systems. The substantial share of foreign beneficiaries in the total number of pensioners implies that it is even more important for Luxembourg than for many other countries to build up substantial financial reserves in the pension system.

A second area of concern is health care. The Government's recent decision to limit the contribution of the central government budget to the health care system is welcome, but the efforts to better control expenditure growth need to be strengthened. Failure to bring the rapid increase in health expenditures under control would make increased taxes or social security contributions unavoidable, as is already evidenced by the need to raise contributions next year.

A third area of concern is state support to the domestic industry. Generous state aid and tax incentives have contributed to the achievement of a more diversified and less vulnerable production structure. However, given the inherent advantages offered by Luxembourg, the substantial production base already established, and the wide range of financing opportunities offered by the financial markets, the high level of subsidies is no longer necessary and involves a significant risk of misallocation of resources.

The debate on continued Luxembourg participation in the monetary association with Belgium has lost much of its immediate relevance with the strengthening of the Belgian franc. The staff agrees that the small size and openness of the economy limit the possibilities of independent monetary and exchange rate policies. Luxembourg is best served by belonging to an area with low inflation and stable financial conditions--that is, in practice, by pegging to a relatively strong currency. Historically, this has been achieved via the monetary association with Belgium. Aside from the exceptionally turbulent period in foreign exchange markets of late summer, this arrangement has generally served Luxembourg well, as the authorities recognize. Looking ahead, Luxembourg's strong fundamentals make it a candidate to be among the first group of countries to proceed to the third stage of EMU.

Luxembourg has benefitted from an open trading regime and it should support further steps to liberalize trade.

Despite considerable recent increases, Luxembourg's share of official development assistance in GDP is still low, particularly in light of the wealth of the country. The staff welcomes the authorities' intention to increase this share substantially.

It is recommended that the next Article IV consultation with Luxembourg be concluded within 24 months of completion of the present Article IV consultation.

Luxembourg - Basic Data

Area:	2,586.4 sq.km.
Population (1992):	395 thousand
GDP per capita (1992):	US$30,000
Population characteristics and health:	
Life expectancy at birth (1985-87)	
Male	70.6 years
Female	77.9 years
Infant mortality (1991)	9.2 per thousand
Population per physician (1991)	506 persons
Population per hospital bed (1991)	89 persons
Population density (1991)	153 persons per sq.km.

National accounts (in current prices): 1/

	1974		1992	
	Lux F billion	Percent of GDP	Lux F billion	Percent of GDP
Private consumption	43.2	43.4	191.0	50.1
Public consumption	10.8	10.8	58.0	15.2
Gross fixed capital formation	23.0	23.1	94.1	24.7
Increase in stocks	-2.7	-2.7	8.3	2.2
Exports of goods and services	99.2	99.7	344.1	90.5
Imports of goods and services	74.0	74.4	314.6	82.6
GDP	99.5	100.0	380.9	100.0

	1989	1990	1991	1992	1993 2/	1994 2/
	(Percentage changes) 3/					
Private consumption	3.9	4.0	6.5	1.7	1.7	2.5
Public consumption	1.9	3.2	3.8	3.4	2.4	2.6
Gross fixed capital formation	8.9	2.5	9.8	-2.2	6.7	-3.5
Increase in stocks 4/	0.7	1.3	0.9	-0.3	-0.7	1.2
Total domestic demand	5.7	5.1	8.0	0.5	2.2	2.3
Exports of goods and services	7.9	4.0	3.1	2.4	1.4	1.1
Imports of goods and services	6.1	4.3	8.1	0.2	1.5	1.3
GDP	7.8	4.6	2.7	2.8	2.0	2.0
Employment	3.7	4.3	4.3	1.9	1.1	...
Unemployment rate (in percent)	1.4	1.3	1.4	1.6	2.0	...
Consumer prices	3.4	3.7	3.1	3.2	3.8	...
Real effective exchange rate	-0.3	1.3	0.5	0.6	-1.8 5/	...
Nominal effective exchange rate	-0.4	2.0	0.4	0.6	-1.5 5/	...
Hourly remuneration	6.9	6.8	6.2	6.0	...	...
In industry	6.4	5.7	6.6	7.3	...	...
Unit labor costs in industry	-2.1	4.9	4.0	5.5	...	...
Wages per employee	6.5	5.2	4.7	5.1	...	...

	1989	1990	1991	1992	1993 2/	1994 2/
Money plus quasi-money 6/	19.8	16.6	11.5	6.6	...	...
Total domestic credit 6/	15.1	19.9	6.7	21.4	...	...
Interest rates: Short-term	7.0	8.3	9.4	9.4	8.5	...
Long-term	7.7	8.5	8.2	7.9	6.8	...
	(In percent of GDP)					
Central government finances 7/						
Revenue	32.7	32.9	31.8	31.8	30.9	31.3
Expenditure	32.4	32.8	32.8	33.0	31.4	31.7
Financial balance	0.3	0.1	-0.3	-1.2	-0.4	-0.4
Consolidated central government balance 8/	2.7	1.8	-2.4	-2.9	-1.8	-1.9
General government 9/						
Revenue	46.5	47.4	45.4	45.0	44.6	...
Expenditure	41.3	42.0	45.9	45.9	45.7	...
Financial balance	5.2	5.4	-0.5	-0.9	-1.1	...
Central government gross debt	4.4	3.2	2.6	3.4	3.7	...
Central government reserves	6.8	6.7	3.9	2.4	1.3	...
	(In billions of Lux F)					
Trade balance	-31.5	-42.3	-62.7	-59.2	...	...
Exports of goods	213.6	211.5	215.0	209.2	...	...
Imports of goods	245.1	253.8	277.7	268.4	...	...
Services balance	100.9	112.8	112.5	122.7	...	...
Exports of services	937.2	1,135.7	1,189.4	1,252.4	...	...
Imports of services	836.3	1,022.9	1,076.9	1,129.7	...	...
Transfer balance	-6.3	-5.8	-7.0	-7.3	...	...
Current account	63.1	64.7	42.8	56.2	...	...
(In percent of GDP)	20.0	19.3	12.0	14.8	...	...

1/ According to national definition, which treats banking services to non-residents as part of exports; by contrast, EU-wide standardized SEC definition treats the whole of banking services as an intermediate input.
2/ Staff projections.
3/ GDP and its components in constant 1985 prices.
4/ Contribution to GDP growth.
5/ January-August.
6/ End-period; change from one year earlier.
7/ Central government including borrowing transactions; 1993 figures refer to voted budget and 1994 figures to budget proposal.
8/ Excluding borrowing and amortization; including special state funds.
9/ Not including municipalities.

Luxembourg: Fund Relations
(As of November 30, 1993)

I. Membership Status: Joined 12/27/45; Article VIII

II. General Resources Account:	SDR Million	% Quota
Quota	135.50	100.0
Fund holdings of currency	111.31	82.1
Reserve position in Fund	24.20	17.9
Operational budget transfers (net)	0.10	

III. SDR Department:	SDR Million	% Allocation
Net cumulative allocation	16.96	100.0
Holdings	6.98	41.2

IV. Outstanding Purchases and Loans: None

V. Financial Arrangements: None

VI. Projected Obligations to Fund : None

VII. Exchange Rate Arrangements

Luxembourg forms a monetary union with Belgium in which the Luxembourg and the Belgian franc are at par. A maximum margin of 15 percent is maintained between the Belgian and Luxembourg francs and the currencies of other countries participating in the exchange rate mechanism of the European Monetary System.

VIII. Exchange Restrictions

Luxembourg continues to apply exchange restrictions vis-à-vis Iraq, which were notified to the Fund under Decision 144-(52/51) on September 4, 1990 (EBD/90/280). Luxembourg has also imposed exchange restrictions vis-à-vis the Federal Republic of Yugoslavia (Serbia/Montenegro).

IX. The Last Article IV Consultation

The staff report for the 1991 Article IV consultation with Luxembourg was considered by the Executive Board at EBM/91/169, December 16, 1991. Directors agreed to keep the next Article IV consultations with Luxembourg on the two-year cycle.