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SM/97/161
Supplement 1

CONTAINS CONFIDENTIAL
INFORMATION

August 5, 1997

To: Members of the Executive Board

From: The Acting Secretary

Subject: **Dominican Republic—Staff Report for the 1997 Article IV Consultation**

The attached supplement to the staff report for the 1997 Article IV consultation with the Dominican Republic (SM/97/161, 6/24/97) has been prepared on the basis of additional information.

Mr. Guzmán (ext. 38606) or Mr. D. Dunn (ext. 38609) is available to answer technical or factual questions relating to this paper prior to the Board discussion scheduled for Wednesday, August 20, 1997.

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 WTO Secretariat on Wednesday, August 13, 1997; and to the European Commission (EC) and the Inter-American Development Bank (IDB), following its consideration by the Executive Board.

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INTERNATIONAL MONETARY FUND

DOMINICAN REPUBLIC

**Staff Report for the 1997 Article IV Consultation
Supplementary Information**

Prepared by the Western Hemisphere and
Policy Development and Review Departments

Approved by Claudio M. Loser and Joaquin Pujol

August 5, 1997

1. Recent data (described below) indicate that economic performance in recent months has been somewhat better than anticipated in the staff report. Moreover, certain recently enacted measures (specified below) suggest that opposition in congress to the administration's structural reform program is subsiding. The staff is encouraged by these developments, which should help the authorities sustain the implementation of prudent macroeconomic policies, while creating a more conducive environment for accelerating structural reforms and gradually redirecting resources to the fulfillment of social needs.
2. Preliminary data indicate that **real GDP** rose by a stronger-than-expected 6½ percent in the first half of 1997 (compared with the same period a year earlier), largely reflecting an acceleration in private construction activity in the second quarter. Construction is expected to continue to be strong in the second half of the year and real GDP is now projected to grow by around 6½ percent for the year as a whole, compared with an earlier projection of around 5 percent. Reflecting the rapid growth of economic activity during the first half of 1997, the rate of unemployment declined from 16.5 percent in October 1996 to 15.6 percent in April 1997. The 12-month rate of consumer price inflation has remained steady at about 7½ percent in recent months and it is now expected to continue at around this level through December 1997.
3. Preliminary information suggests that the central government registered a surplus and the **consolidated public sector finances** (including quasi-fiscal operations) were near equilibrium in the first half of 1997. Tax revenue increased by more than had been anticipated earlier, reflecting strong output growth and continued improvements in tax administration. Taking into account recent revenue trends and assuming expenditure restraint in the remainder of this year, the staff now projects that the consolidated public sector deficit could decline from 1.7 percent of GDP in 1996 to near ½ percent of GDP in 1997.

4. **Private sector minimum wages** in the industrial free trade zones recently were increased by 15 percent effective June 1997. The employers' association increased unilaterally other private sector minimum wages by the same percentage in July, while discussions covering additional increases in these wages continue in the National Salary Commission.

5. The growth of **money and credit** to the private sector slowed during the first half of the year. Banking system liabilities to the private sector expanded by 10 percent in the year to June 1997, while credit to the private sector expanded by 15 percent (compared with 20 percent and 24 percent, respectively, during 1996). Nominal interest rates on 60-day loans and deposits declined by ½ percent during the first half of the year.

6. In U.S. dollar terms, the **trade account deficit** widened in the first half of 1997 (relative to the same period a year earlier) as non-free trade zone imports expanded by 10 percent, nonfree trade zone exports by 2½ percent and net exports from free trade zones by 8½ percent. The widening of the trade account deficit, however, was largely offset by a 20 percent increase in travel receipts, and the external current account deficit is estimated to have remained at about the level of the same period of the previous year. During the first half of 1997, the central bank's net international reserves increased by about US\$35 million and its gross international reserves rose by about US\$15 million. The official market exchange rate has remained constant in recent months, and the spread between it and the commercial banks market rate recently has declined to around ½ percent. Revised projections suggest that official net international reserves may increase by about US\$90-120 million and gross international reserves by about US\$20-50 million during 1997; moreover, international reserves may rise by an additional US\$100 million if the sale of certain real estate assets held by the central bank takes place before year-end.

7. Progress has been made in the **structural area** in recent weeks. Legislation for the restructuring and partial privatization of the public enterprises was passed by congress and signed into law in late June, which strengthens the legal framework for the planned divestment of certain assets and operations of the loss-making electricity and sugar companies before year-end. Preparatory work is also underway for the granting of concessions for private investment in ports and airports and other basic infrastructure and services in 1998. In addition, congress recently approved legislation that would allow disbursements of external loans from the European Investment Bank, the Inter-American Development Bank, and the World Bank to finance electrical power transmission, irrigation and highway projects. Following discussions with labor union leaders in early July, the President announced his intention to allow union participation in the reform and capitalization of the public enterprises and to submit this year a proposal to congress for social security reform, including private sector participation in a pension scheme of fully capitalized individual retirement accounts.