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EBS/85/75

CONFIDENTIAL

March 27, 1985

To: Members of the Executive Board

From: The Acting Secretary

Subject: Dominican Republic - Request for Stand-By Arrangement and Approval of Exchange Restrictions

Attached for consideration by the Executive Directors is a paper on a request from the Dominican Republic for a stand-by arrangement equivalent to SDR 78.5 million. Draft decisions appear on page 24.

This subject, together with the background paper on the exchange arrangements and exchange system of the Dominican Republic (EBS/85/76, 3/27/85), will be brought to the agenda for discussion on a date to be announced.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. McLoughlin, ext. 8484.

Att: (1)

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

DOMINICAN REPUBLIC

Request for Stand-By Arrangement and Approval of Exchange Restrictions

Prepared by the Western Hemisphere Department

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

Approved by Eduardo Wiesner and Manuel Guitián

March 26, 1985

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I. Introduction

Discussions on a financial program for 1985 took place in Santo Domingo and Washington, D.C., during the period October 1984-February 1985. The Dominican representatives included the Governor of the Central Bank, the Technical Secretary of the Presidency, the Secretary of Finance, the Economic Advisor of the President, as well as senior officials concerned with economic and financial matters. The staff representatives, who participated in one or more rounds of the discussions, were Mr. J. Gonzalez (Head), Mr. E. Decarli, Mr. T.P. McLoughlin, Mr. R. Incer, (all WHD), Mrs. M. Tyler (ETR), Ms. E. Milne (RES), Mr. P. Shome (FAD), Ms. N. Wise (Secretary-INST), and Ms. G. Ulmschneider (Secretary-WHD). Mr. A. Kafka, Executive Director, participated in some of the discussions.

In the attached letter dated February 28, 1985 the Governor of the Central Bank requests access to Fund resources in an amount equivalent to SDR 78.5 million, or 70 percent of the quota of the Dominican Republic, within the framework of a one-year stand-by arrangement. The entire amount requested under the arrangement would come from ordinary resources. The proposed phasing of purchases is shown in Table 1.

As of February 28, 1985, the Fund's holdings of Dominican Republic pesos, subject to repurchase, amounted to SDR 225.7 million, or 201 percent of quota. Full use of the requested resources under the stand-by arrangement would raise the Fund's holdings of Dominican Republic pesos to SDR 267.5 million, or 239 percent of quota. Accordingly, a waiver of the limitation in Article V, Section 3(b)(iii) of the Articles of Agreement, is required. Further information on the Dominican Republic's relations with the Fund is presented in Appendix I. Basic data for the Dominican Republic are presented in Appendix II. Relations with the World Bank group are presented in Appendix III. A companion paper "Dominican Republic--Exchange Arrangements and Exchange System" (EBS/85/76, 3/27/85) discusses recent changes in the exchange system.

II. Summary of Recent Developments

In recent years the Dominican Republic has experienced widening external and internal imbalances (Table 2). While these disequilibria stemmed in part from adverse external developments, including the sharp rise in oil prices, unfavorable movements in the terms of trade, and rising interest rates, they were attributable to a large extent to the pursuit of inappropriate policies.

The Government that took office in August 1982 adopted a three-year economic program covering the period 1983-85, a program which was supported by an extended arrangement from the Fund in the amount of SDR 371.25 million, or 450 percent of the then quota. This arrangement was approved by the Executive Board on January 21, 1983.

Table 1. Dominican Republic: Projected Purchases and Scheduled Repurchases
(April 1985-April 1986)

	Outstanding	1985				1986	
	Feb. 28, 1985	Jan.-Mar.	Apr.-June	July-Sept.	Oct.-Dec.	Jan.-Mar.	April
			(In millions of SDRs)				
Transactions under tranche policies (net)	--	--	28.0	16.7	16.7	17.1	--
Purchases	--	--	28.0	16.7	16.7	17.1	--
Repurchases	--	--	--	--	--	--	--
Transactions under special facilities (net) 1/	225.7	-23.2 2/	--	-4.5	-4.5	-4.5	-5.3
Total Fund credit outstanding (end of period)	225.7	202.5	230.5	242.7	254.9	267.5	262.2
Under tranche policies	--	--	28.0	44.7	61.4	78.5	78.5
Special facilities	225.7	202.5	202.5	198.0	193.5	189.0	183.7
			(As percent of quota)				
Total Fund credit outstanding (end of period)	201.3	180.6	205.6	216.5	227.4	238.6	233.9
Under tranche policies	--	--	25.0	39.9	54.7	70.0	70.0
Special facilities	201.3	180.6	180.6	176.6	172.7	168.6	163.9

Source: IMF Treasurer's Department.

1/ Includes outstanding use under EFF.
2/ Early repurchase under Buffer Stock Financing Facility (sugar).

Table 2. Dominican Republic: Selected Economic and Financial Indicators, 1981-85

	1981	1982	1983	Prel. 1984	Proj. 1985
	(Annual percentage changes, unless otherwise specified)				
National income and prices					
GDP at constant prices	4.1	1.6	3.9	1.0	2.0
GDP at current market prices	9.1	9.0	11.4	18.7	23.4
GDP deflator	4.8	7.3	7.2	17.5	21.0
Consumer prices (average)	7.5	7.6	6.9	24.4	24.0
External sector (on the basis of U.S. dollars)					
Exports, f.o.b.	23.5	-35.4	2.3	10.0	-7.4
Imports, f.o.b.	-4.5	-13.4	2.0	-2.1	-8.4
Export volume	10.9	-26.4	-0.3	4.9	0.3
Import volume	-7.5	-14.6	--	-3.0	-9.0
Terms of trade (deterioration -)	4.1	-13.4	0.6	4.0	-8.4
Effective exchange rate 1/					
Nominal	4.9	-1.1	-6.6	-38.7	...
Real	1.6	-0.9	-6.9	-27.8	...
Central Government					
Revenue	4.0	-18.5	22.3	19.6	95.1
Expenditure	0.3	-10.0	17.4	12.7	86.7
Money and credit 2/					
Domestic credit 3/	28.2	45.4	34.5	30.2	16.8
Public sector (net) 3/	(32.5)	(32.5)	(23.2)	(8.7)	(--)
Private sector 3/	(-2.3)	(8.0)	(6.6)	(10.5)	(17.7)
Money and quasi-money (M2)	11.9	15.4	7.8	28.0	24.0
Velocity (GDP relative to M2)	6.1	5.8	6.0	5.8	5.8
	(In percent of GDP) 4/				
Overall consolidated public sector deficit	-6.2	-6.2	-5.6	-7.5 5/	-4.9 6/
Overall nonfinancial public sector deficit	...	...	...	-4.9	-4.9
Gross domestic investment	24.3	20.8	21.4	20.5	21.7
Gross national savings	18.7	15.2	15.4	16.2	21.1
BOP-current account deficit	-5.6	-5.6	-6.0	-4.3	-0.6 6/
External public debt 7/	25.7	26.1	38.1	55.0	57.8
	(In percent of exports of goods and nonfactor services)				
Debt service	32.8	43.0	49.1	47.2	63.8
Of which: interest payments	(20.2)	(25.0)	(24.7)	(19.3)	(16.8) 6/
	(In millions of U.S. dollars)				
Overall balance of payments	-109.6	-356.3	-352.7	-154.7	-149.6
Change in net international reserves (increase -)	109.6	356.3	58.2 8/	-92.2 9/	-108.7 10/
Arrears (decrease -)	--	--	142.6	246.9	-77.5
Other 11/	--	--	151.9	--	335.8
Gross official reserves	283.5	172.4	204.3	268.0	295.0
(weeks of imports)	(10.3)	(7.1)	(8.1)	(11.1)	(13.3)

Sources: Central Bank of the Dominican Republic; and Fund staff estimates and projections.

1/ Based on a composite exchange rate which reflects non-oil transactions in the official and parallel markets.
2/ Excludes nonbank financial intermediaries.
3/ Changes in relation to broad money outstanding at the beginning of the period.
4/ In terms of U.S. dollars; prior to 1983 foreign transactions are accounted at the rate of RD$1 per U.S. dollar, in 1983 at the rate of RD$1.3 per U.S. dollar, in 1984 at the rate of RD$2 per U.S. dollar, and in 1985 at the rate of RD$2.8 per U.S. dollar.
5/ Includes central bank losses of RD$270.3 million.
6/ Before debt relief.
7/ Debt of all maturities, including use of Fund credit, but excluding other reserve liabilities of the Central Bank.
8/ During the year there was an accumulation of unpaid external obligations outside the Central Bank as well as debt relief.
9/ During the year there was a further accumulation of unpaid external obligations outside the Central Bank.
10/ A financing gap for this year is in prospect before debt relief.
11/ Includes debt relief in 1983 and the financing gap in 1985.

The key feature of the economic program was a commitment to a strengthening of fiscal and monetary policies, adjustment of the exchange rate of the peso,1/ reform of the exchange system, and the implementation of an adequate public investment program combined with incentives for private investment. For 1983, the main objectives of the program included a sharp reduction in the public sector deficit, a strengthening of the external position, and an increase in investment. Moreover, credit policy was formulated with a view to slowing the growth of liquidity in the economy.

In the early stages of the program, progress was made in redressing existing imbalances. Moreover, the Dominican Republic began negotiations for debt relief with commercial banks, and there was a partial restoration of confidence, as evidenced by a sharp reduction in capital outflows. The Dominican Republic observed all performance criteria through September 1983 and purchased the total of SDR 123.8 million. However, the overall performance of the Dominican economy during the year was not in accordance with the targets envisaged in the program and the desired degree of adjustment did not take place.2/

A major area of slippage was public finance. While fiscal policy began to depart from the program track before midyear, the slippage was heavily concentrated in the last months of 1983 and the ratio of the fiscal deficit to GDP reached some 5.6 percent, compared with a program target of 3.9 percent. The deviations in the fiscal area were compounded by departures from program targets in other areas, which aggravated pressures on the balance of payments. After approaching the Paris Club with a request for rescheduling in August 1983, the Dominican Republic suspended payments to official creditors. The agreement on refinancing with commercial banks was not reached until December 1983, and amortization payments were not made as planned. Thus, in 1983 external arrears (including those within the Central Bank) rose by a further US$210 million; the overall balance of payments deficit remained at more than US$350 million, virtually unchanged from the 1982 level; and the peso depreciated sharply in the parallel foreign exchange market in the second half of the year.

At the time discussions between the staff and the authorities were initiated to define policies for the second year of the extended arrangement in October 1983, it was apparent that the program was off track and accordingly these discussions focused on dealing with the slippages observed in the first year of the extended arrangement. However, in successive rounds of intensive discussions, it did not prove possible to reach understandings on a program for 1984. One major obstacle was the implicit subsidy granted to consumers of petroleum products through importing oil at the official exchange rate.

1/ The currency of the Dominican Republic is the peso. Since January 23, 1985 the peso has been floating freely.

2/ Performance under the program for the first year of the extended arrangement was described in detail in the Staff Report for the 1984 Article IV Consultation (SM/84/161, 7/5/84, pp. 11-13).

As uncertainty mounted about the timely implementation of adjustment measures, the peso came under renewed pressure in the parallel market in late 1983 and the early months of 1984, depreciating to around RD$2.8 per U.S. dollar (buying) in February from around RD$1.84 per U.S. dollar in November 1983.

The authorities began to implement measures directed toward unification of the exchange system in early 1984. In April, all payments for current transactions other than for petroleum imports and interest payments on the external debt, as well as letters of credit and other outstanding obligations of the Central Bank, were transferred to the parallel market. Almost all nontraditional exports were effectively transferred to the parallel market and traditional exports and services were granted more favorable exchange rate treatment. Domestic prices of many basic foodstuffs and other products subject to price control were adjusted to reflect these exchange rate measures.

In August 1984 an "intermediate" exchange rate was established for oil imports (other than those of the Electricity Corporation) and the prices of petroleum products were raised by more than 60 percent. A number of other revenue measures also were taken and public investment projects were cut back. On a cash basis, the overall deficit of the nonfinancial public sector in 1984 was contained to RD$328 million. However, during the year the Central Bank incurred substantial losses which reflected to a large extent the effects of the overvalued exchange rate of the peso and interest payments on foreign debts it assumed in December 1983. When these losses were consolidated with the fiscal accounts, the combined overall deficit reached RD$598 million, equivalent to 7.5 percent of GDP in 1984.

The balance of payments outcome improved somewhat in 1984. The current account deficit was nearly halved, in large part because of a significant recovery in export and tourism receipts, and there was a reduction in the overall deficit from US$353 million in 1983 to US$155 million in 1984. However, external payments arrears more than doubled, to some US$500 million at the end of 1984. As a result of the depreciation of the effective exchange rate of the peso and the corrective price adjustments, prices rose 24 percent on an average annual basis in 1984 compared with 7 percent in 1983. The rate of growth of real GDP declined from 4 percent in 1983 to an estimated 1 percent in 1984.

III. The Program for 1985

By late 1984 it was concluded that a program for 1985 could best be formulated in the context of a one-year stand-by arrangement. In light of the progress being made in this direction, the Dominican authorities formally canceled the extended arrangement on January 17, 1985.

The financial program for 1985 seeks to strengthen the country's external position and contain the rate of inflation while creating the conditions for renewed economic growth. These objectives are to be achieved through the adoption of realistic exchange rate and pricing policies, combined with restrained fiscal and monetary policies. To this end, the exchange system was unified on January 23, 1985.1/ Since then the peso has been floating and the rate has been determined by the free play of market forces. At the same time, adjustments were made in the prices of petroleum products, electricity tariffs, and other controlled prices.

On the basis of these policies, the authorities expect to achieve in 1985 a cutback in the deficit of the public sector to less than 5 percent of GDP, a reduction in the deficit in the current account of the balance of payments before debt relief to only about 0.6 percent of GDP (US$29 million), an increase in the net international reserves of the Central Bank of some US$109 million, and an increase in real GDP of about 2 percent. The Dominican Republic expects to reach agreement with the official creditors of the Paris Club to refinance debt service payments falling due during the year, as well as a refinancing agreement for 1985 obligations with commercial banks. A summary of the main elements of the program is presented in Appendix IV.

1. Fiscal policy

The program calls for reducing the ratio to GDP of the overall deficit of the nonfinancial public sector to 4.9 percent in 1985, from an average of about 6.4 percent 2/ in the four-year period ended 1984. Comparisons between fiscal policy in 1985 and earlier years are complicated by the fact that in 1985 all calculations are based on an accounting exchange rate of RD$2.8 per U.S. dollar, whereas in previous years the budgets were based on the official parity of RD$1 per U.S. dollar.3/

In 1985 total revenue of the consolidated nonfinancial public sector is projected to rise by 75 percent to RD$2.2 billion (Table 3). The principal discretionary measure taken was the imposition of exchange taxes of 36 percent and 5 percent on most traditional and nontraditional export receipts (goods and services), respectively. The authorities have indicated that this measure is intended to be temporary and that it will be replaced by permanent fiscal measures. The exchange tax is projected to yield some RD$712 million, accounting for about two thirds

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1/ The formal legal ratification of the new exchange rate system has not yet taken place (EBS/85/76 , 3/27/85).
2/ Includes the operating losses of the Central Bank in 1984.
3/ The accounting rate of RD$2.8 per U.S. dollar for 1985 was thought to be realistic, provided the adjustment measures were in place. During the first two months of 1985 the actual exchange rate has been in the region of RD$3.25 per U.S. dollar.

Table 3. Dominican Republic: Public Sector Operations, 1981-85

	1981	1982	1983	Prel. 1984	Proj. 1985
	(In millions of Dominican pesos)				
Total revenue	933.3	783.1	924.8	1,234.6	2,156.3
Central Government 1/	926.0	752.8	923.2	1,089.2	2,153.4
Current	(909.2)	(743.3)	(917.4)	(1,082.9)	(2,146.9)
Capital	(16.8)	(9.5)	(5.8)	(6.3)	(6.5)
Public enterprises 1/	7.3	30.3	1.6	145.4	2.9
Operating surplus	(--)	(--)	(--)	(143.8)	(--)
Capital revenue	(7.3)	(30.3)	(1.6)	(1.6)	(2.9)
Total expenditure	1,286.3	1,199.9	1,319.6	1,494.8	2,750.0
Central Government 1/	1,058.1	942.3	1,081.5	1,281.4	2,002.8
Current expenditure	(755.0)	(760.1)	(863.5)	(1,025.6)	(1,580.4)
Capital expenditure	(303.1)	(182.2)	(218.0)	(255.8)	(422.4)
Of which: capital formation	/151.8/	/110.7/	/130.7/	/156.0/	/401.8/
Public enterprises 1/	228.2	257.6	238.1	213.4	747.2
Operating loss	(63.2)	(57.1)	(74.4)	(--)	(1.1)
Interest payments	(50.9)	(71.9)	(82.4)	(53.2)	(168.4)
Capital expenditure	(114.1)	(128.6)	(81.3)	(160.2)	(577.7)
Of which: capital formation	/81.8/	/123.2/	/68.9/	/138.9/	/571.2/
Overall deficit of the consolidated public sector	-353.0	-416.8	-394.8	-260.2	-593.7
Overall deficit of the nonconsolidated public sector	-95.4	-75.4	-68.7	-68.0	-36.3
Overall deficit (-)	-448.4	-492.2	-463.5	-328.2	-630.0
Financing	448.4	492.2	463.5	328.2	630.0
External	105.6	108.6	113.0	186.2	630.0
Domestic	342.8	383.6	350.5	142.0	--
Banking system	(342.8)	(383.5)	(315.5)	(127.3)	(--)
Other 2/	(--)	(0.1)	(35.0)	(14.7)	(--)
Memorandum items					
Consolidated deficit	...	...	...	-598.5	-630.0
Deficit of nonfinancial public sector	(...)	(...)	(...)	(-328.2)	(-630.0)
Operating losses of the Central Bank	(...)	(...)	(...)	(-270.3)	(--)
Financing gap	...	...	...	...	1,267.3
Overall deficit	(...)	(...)	(...)	(...)	(630.0)
Scheduled amortization	(...)	(...)	(...)	(...)	(637.3)
Consolidated deficit (as percent of GDP)	-6.2	-6.2	-5.6	-7.5	-4.9

Sources: Data provided by the Dominican authorities; and Fund staff estimates and projections.

1/ Totals may differ from data in Table 9 of Appendix V and Statistical Appendix Table 13 as a result of transfers which are netted out in the consolidation process.

2/ Change in cash balances, items in transit, bonds of the National Housing Institute (INVI), and other.

of the rise in total revenue of the Central Government.1/ Higher prices for petroleum products are expected to yield a further RD$184 million in tax revenue, or 17 percent of the increase in revenue of the Central Government. An additional RD$100 million, or 10 percent of the growth in revenue, will be generated from customs duties since these now will reflect the importation of goods at the actual exchange rate rather than the accounting rate of RD$2 per U.S. dollar in effect since August 1984. Thus, 94 percent of the increase in central government revenue in 1985 is projected to come from discretionary measures already implemented, and the remainder will be obtained from improved collection procedures as well as the normal growth in the revenue base.

Total expenditure of the nonfinancial public sector is projected to rise by 84 percent in 1985 to RD$2.7 billion. Current expenditure of the Central Government is programmed to rise by 54 percent to RD$1.6 billion, largely because implicit subsidies are being transformed into expenditure since a more appropriate exchange rate is being used for accounting purposes. The authorities have announced that there will be no adjustment in salaries and no year-end bonus for government employees unless Congress passes compensating revenue or expenditure measures. Capital expenditure is projected to rise by 65 percent to RD$422 million in 1985, with most of the increase also being due to the exchange rate action.

In the case of the largest public enterprises (CDE, INESPRE, CEA, and CORDE), however, a significant increase is expected in the overall deficit, from RD$77 million in 1984 to RD$344 million in 1985 (Appendix V). The larger deficit derives essentially from the higher foreign exchange costs associated with the investment plan of the Electricity Corporation; this plan is an essential element in improving the financial performance of the enterprise over the medium term and in lessening the country's dependence on imported petroleum products. The program provides for major price adjustments in the case of the principal loss-making public enterprises. Thus, electricity tariffs have been raised by 50 percent, on average, and large increases have been announced in the case of foodstuffs sold by INESPRE. Moreover, the activities of INESPRE have been scaled down.

2. Monetary and credit policies

The authorities have recognized that the need to strengthen the foreign reserve position of the Central Bank while providing adequate credit to the private sector has precluded the extension of net bank credit to the public sector in 1985. Accordingly, the fiscal measures

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1/ For analytical purposes, the proceeds of the tax are presented as budgetary revenue. The taxes are actually levied on export proceeds; prior to unification of the exchange rate there was an implicit tax on traditional exports at an even higher rate, resulting from the difference between the exchange rate of RD$1.48 per U.S. dollar used for surrender purposes and the free market rate which averaged RD$2.8 per U.S. dollar during 1984. The proceeds from the differential were used to subsidize petroleum imports and other official transactions.

described above have been aimed at reducing the financing gap of the nonfinancial public sector to a level compatible with the amount of foreign financing expected to be available; the public sector will make no use of domestic bank financing other than for strictly seasonal purposes. Credit to the private sector, whose financing needs will increase significantly as a result of the exchange rate action, is projected to rise by 23 percent. The program calls for an increase in the net foreign assets of the Central Bank of some US$109 million, while the net domestic assets of the Central Bank would decline by some RD$165 million during 1985 (Table 4 and Statistical Appendix Table 14). The rate of increase of the money supply which had been 28 percent in 1984 is projected to decelerate to 24 percent in 1985, a rate of expansion which would be roughly in line with the rise in nominal GDP.

To promote the flow of private financial savings and ensure an efficient allocation of financial resources, the authorities are intensifying their efforts to strengthen the financial system and increase the flexibility of interest rates. As an important step in this direction, the terms on which financial institutions can issue financial certificates were liberalized significantly in January 1985. Previously, these certificates had been issued in denominations of RD$100,000, with maturities of 1-3 years, and carried interest rates of 10-14 percent. Now, the minimum denomination of these certificates has been lowered to RD$10,000, the minimum term set at 180 days, and interest rates can be negotiated in the range of 9 1/2-18 percent. Moreover, certain lending rates have also been effectively increased.

In order to ensure better control over the expansion of domestic liquidity, the Central Bank is taking the following measures during 1985.

(a) The placement in the market of RD$100 million of stabilization bonds.

(b) The establishment of a marginal reserve requirement of 100 percent on the increase in sight, time, and savings deposits of the commercial banks over the average of these deposits during the last quarter of 1984.

(c) The freezing of the Central Bank's discount operations to the level existing at end-1984 and a reduction of 10 percent for the commercial banks and 5 percent for the financial institutions after the first renewal of the discount lines.

(d) An increase in the discount rates from a range of 6.5 to 9 percent to a level of 12 percent, and an increase in the rate charged on the Special Development Fund (FIDE) operations with the financial intermediaries to 12 percent.

(e) An increase in the rate charged by the Central Bank to FIDE to 6 percent.

Table 4. Dominican Republic: Summary Accounts of the Central Bank, 1981-85

(In millions of Dominican pesos)

	1981	1982	1983	Prel. 1984	Prel. 1984 1/	Proj. 1985 1/
Net international reserves	-322.3	-678.6	-428.1	-335.9	-940.5	-636.1
Assets	283.5	172.4	204.3	268.0	750.4	826.0
Liabilities	-605.8	-851.0	-632.4 2/	-603.9	-1,690.9	-1,462.1
Net domestic assets	718.2	1,109.8	915.0	1,027.6	1,632.2	1,467.4
Claims on the public sector (net)	688.0	970.5	1,253.8	1,333.3	1,333.3	1,333.3
Central government	(536.1)	(732.0)	(916.1)	(935.4)	(935.4)	(935.4)
Public financial institutions	(146.5)	(151.2)	(149.6)	(148.0)	(148.0)	) (148.0)
Rest of public sector	(5.4)	(87.3)	(188.1)	(249.9)	(249.9)	) (249.0)
Credit to commercial banks (net)	-39.8	201.1	301.9	244.8	244.8	155.5
Credit to rest of the financial system	133.0	157.9	190.7	215.9	215.9	215.9
Medium- and long-term foreign liabilities	-259.0	-359.1	-829.4	-878.4	-2,459.5	-2,547.7
Revaluation account	--	--	--	--	2,185.7	2,185.7
Net unclassified assets	196.0	139.4	-2.0	112.0	112.0	124.7
Currency issued	395.9	431.2	486.9	691.7	691.7	831.3
Currency in circulation	323.8	357.1	414.7	592.8	592.8	724.2
Cash in vaults	72.1	74.1	72.2	98.9	98.9	107.1

Sources: Central Bank of the Dominican Republic; and Fund staff estimates and projections.

1/ Foreign currency items valued at RD$2.8 per U.S. dollar.
2/ In December 1983 a total of US$309.7 million of Central Bank foreign reserve liabilities was converted into a medium-term loan as a result of a refinancing agreement with commercial banks.

The financial position of the Reserve Bank (the state-owned commercial bank) has been of concern for some time, especially as regards its failure to meet reserve requirements. While it would be very difficult to bring the Reserve Bank in full compliance with reserve requirements immediately, the authorities have established a timetable for the progressive elimination of the reserve deficiency on existing deposits. A ceiling of RD$125 million on the deficiency of the reserve requirement has been established. Furthermore, the Reserve Bank must comply fully with reserve requirements on additional deposits after December 31, 1984. In the event that the Reserve Bank makes use of overdraft facilities, it will be required to pay penalty rates.

While prices in the first few months of 1985 are expected to increase rapidly as the effects of the corrective adjustments announced in January work through the economy, the rate of price increase in the subsequent months should decline considerably, especially in view of the restrictive monetary policies being pursued. Thus, for the year as a whole, it is expected that the rate of inflation will be contained to about 24 percent on average and that the rate of return on financial assets will turn positive in the course of the year.

3. External policies

As noted earlier, the unification of the exchange system at a rate freely determined by the market is a major element in the program for 1985. In the six weeks since unification took effect on January 23, 1985 the exchange rate of the peso has fluctuated in a range of RD$3.25 to RD$3.3 per U.S. dollar (buying), compared with a rate of RD$3.1 per U.S. dollar prevailing in the parallel market in the preceding 6-8 weeks. In the period from the third quarter of 1983 to the fourth quarter of 1984, the real effective exchange rate of the peso depreciated by 28 percent, and during the fourth quarter of 1984 it was 31 percent below the level of 1980 (Chart and Statistical Appendix Table 19). Most of the depreciation reflected the impact of decisions taken by the authorities to shift additional transactions, in particular imports, from the official to the parallel market.

The balance of payments projections for 1985, before debt relief, call for a sharp reduction in the current account deficit from an estimated 4.3 percent of GDP in 1984 to 0.6 percent in 1985; this is to take place despite an expected adverse movement of some 8 1/2 percent in the terms of trade, stemming mainly from an 8 percent decline in export prices (Table 5 and Statistical Appendix Table 15). Export receipts in 1985 are forecast to fall by 7 percent to US$800 million, while the restrictive demand management policies will result in a reduction in the value of imports by more than 8 percent to US$1,150 million, implying a decline in volume of 9 percent. This decline will reflect essentially reductions in fuel imports, which were unusually high due to stockpiling in 1984, and in imports of consumer goods (Statistical Appendix Table 17). While the trade deficit is projected to decline by US$40 million in 1985 to US$350 million, the services

Table 5. Dominican Republic: Summary Balance of Payments, 1981-85

(In millions of U.S. dollars)

	1981	1982	1983	Prel. 1984	Proj. 1985
Current account	-405.9	-442.0	-421.1	-226.1	-29.3
Trade balance	-263.7	-489.7	-497.0	-391.1	-350.0
Exports, f.o.b.	(1,188.0)	(767.6)	(785.2)	(863.9)	(800.0)
Imports, f.o.b.	(-1,451.7)	(-1,257.3)	(-1,282.2)	(-1,255.0)	(-1,150.0)
Services (net)	-335.2	-157.3	-139.1	-102.3	5.7
Receipts	(336.4)	(378.5)	(451.5)	(534.2)	(609.0)
Of which: travel	/206.3/	/266.1/	/320.0/	/402.9/	/477.7/
Payments	(-671.6)	(-535.8)	(-590.6)	(-636.5)	(-603.3)
Of which: interest	/-304.9/	/-285.5/	/-304.0/	/-268.5/	/-236.2/
Transfers (net)	193.0	205.0	215.0	267.3	315.0
Private	(176.3)	(190.0)	(195.0)	(210.0)	(215.0)
Public	(16.7)	(15.0)	(20.0)	(57.3)	(100.0)
Capital account	296.3	85.7	68.4	71.4	-120.3
Direct investment	79.7	-1.4	22.0	68.5	42.0
Medium- and long-term loans (net)	153.6	150.5	24.1	16.0	-143.0
Drawings	(320.2)	(355.8)	(248.7)	(305.8)	(280.0)
Amortization	(-166.6)	(-205.3)	(-224.6)	(-289.8)	(-423.0)
Other 1/	63.0	-63.4	22.3	-13.1	-19.3
Overall balance	-109.6	-356.3	-352.7	-154.7	-149.6
Financing	109.6	356.3	352.7	154.7	149.6
Net foreign assets of the Central Bank (increase -)	109.6	356.3	58.2 2/	-92.2	-108.7
Assets	(-8.3)	(111.1)	(-31.9)	(-63.7)	(-27.0)
Liabilities	(117.9)	(245.2)	(90.1)	(-28.5)	(-81.7)
Use of Fund credit	/-25.5/	/48.6/	/174.6/	/-25.1/	/29.2/
Arrears	/166.8/	/119.9/	/-67.4/	/34.3/	/-12.5/
Other liabilities	/-23.4/	/76.7/	/-17.1/	/-37.7/	/-98.4/
Arrears 3/ (decrease -)	--	--	142.6	246.9	-77.5
Debt relief	--	--	151.9	--	...
Financing gap	--	--	--	--	335.8

Sources: Data provided by the Central Bank of the Dominican Republic; and Fund staff estimates and projections.

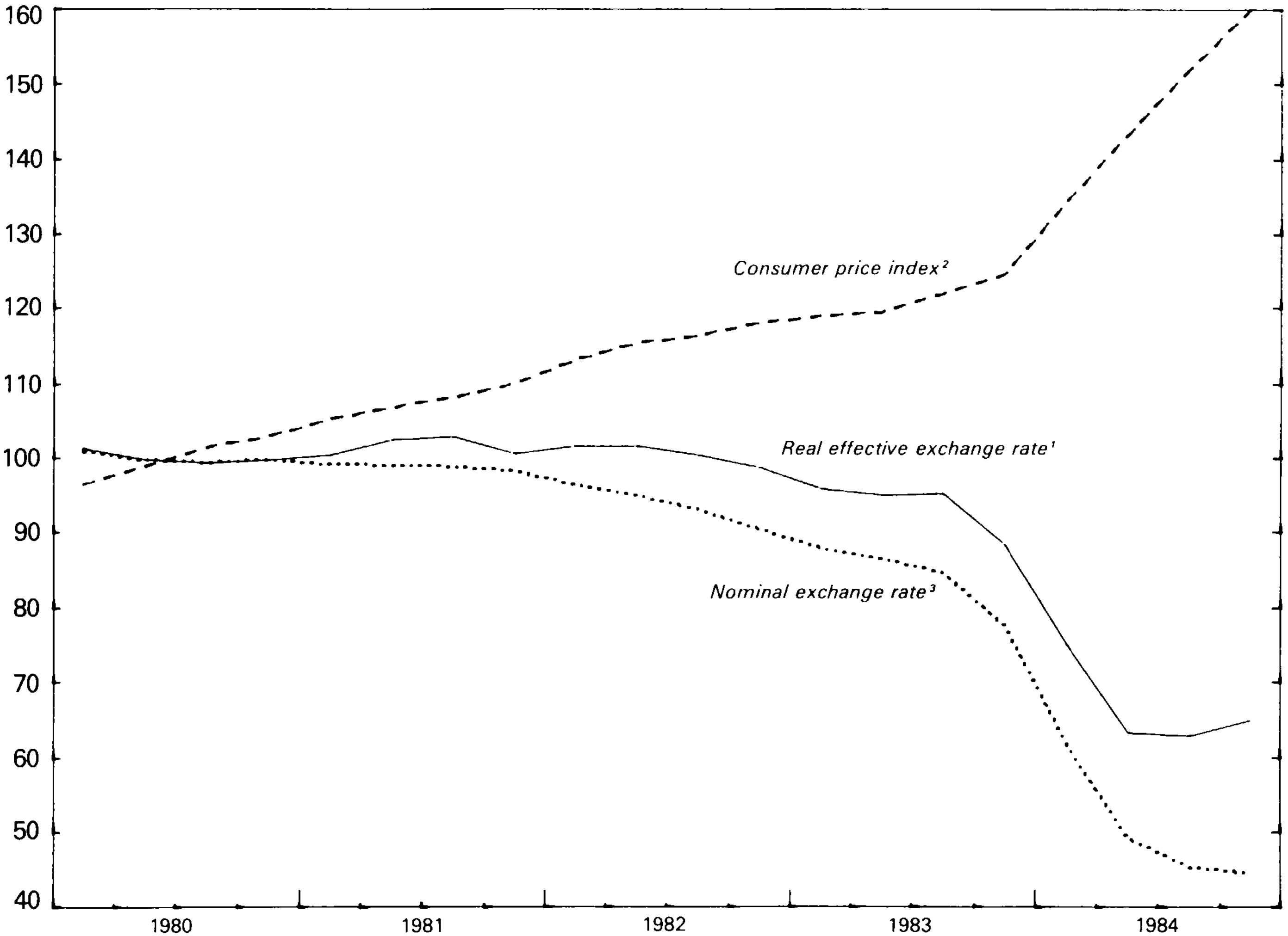
1/ Includes SDR allocation in 1981, short-term public and private capital (net), gold revaluation and monetization, and errors and omissions (net) through 1984.
2/ In December 1983 an amount of US$309.7 million of central bank reserve liabilities was converted into a medium-term loan as a result of a rescheduling with commercial banks.
3/ Outside the Central Bank.

CHART

DOMINICAN REPUBLIC

REAL EFFECTIVE EXCHANGE RATE AND RELATED SERIES

(1980 = 100)



Source: Information Notice System

[1] Trade weighted index of nominal exchange rate deflated by seasonally adjusted consumer price; increase means appreciation.

[2] Seasonally adjusted

[3] U.S. dollars per Dominican peso(composite index)

account is expected to shift into surplus, a turnaround of almost US$110 million. Travel receipts, which had risen by 26 percent in 1984, are forecast to rise by 19 percent while interest payments, before debt relief, are to decline due to the lower level of world interest rates and a reduction in the reserve liabilities of the Central Bank. A significant rise in the net inflow of unrequited transfers is projected, largely as a result of increased foreign assistance.1/

In view of the debt servicing difficulties experienced in recent years, the program places strict limits on disbursements of nonconcessional public sector loans in 1985. Moreover, the tight stance of fiscal policy has resulted in the curtailment of a number of investment projects. Because the first repayments under the 1983 refinancing agreement with commercial banks fall due in 1985, there is a pronounced bunching of amortization payments in 1985. As there will be a decline in drawing on medium- and long-term loans and an outflow of short-term capital, the overall movements on the capital account (before debt relief) will be negative in an amount of US$120 million. The overall balance of payments deficit (before rescheduling) in 1985 is projected to remain at around US$150 million.

Given the target of reducing net foreign liabilities of the Central Bank by US$109 million and external arrears through cash payments in the amount of US$78 million, there is a gap of US$336 million. This gap is expected to be filled by debt relief from the Paris Club creditors and the commercial banks. The progress made in obtaining the envisaged amounts of debt relief will be assessed at the time of the mid-term review with the Fund.

Since the exchange markets were unified on January 23, 1985, all exchange transactions are being carried out at an exchange rate determined freely by the market. The Central Bank buys foreign exchange solely (a) on its own account, to cover its own needs, including compliance with the net foreign assets targets in the program, and (b) on account of the Government, to service the public sector foreign debt and to pay for oil imports. The Central Bank does not intervene in the market for the purpose of influencing the exchange rate. Traditional exports and certain service exports are receiving the market exchange rate minus a temporary exchange tax of 36 percent, and exports of nontraditional goods are receiving the market rate less a temporary exchange tax of 5 percent.

The Dominican Republic retains a number of exchange restrictions subject to Fund approval. These include external payment arrears, a restriction on profit remittances not transferred before January 23, 1985, and a multiple currency practice resulting from a tax on profit

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1/ Available information indicates that the bulk of official transfers in 1985 will be intermediated through a development fund in the Central Bank to finance private sector investment activities. During the course of the review with the Fund the operational aspects of these transactions will be examined.

remittances, including a surcharge on the amount of the tax. The exchange taxes imposed on January 23, 1985 also constitute multiple currency practices subject to Fund approval. In addition, central bank operations in the exchange market at average buying and selling rates determined by reference to the preceding five working days could give rise to a further multiple currency practice in certain circumstances. The authorities will monitor the implementation of these operations with a view to seeking to avoid the development of excessive spreads or broken cross rates. A detailed description of the changes made in the exchange system on January 23, 1985 is contained in EBS/85/76 (3/27/85).

4. Performance criteria and mid-term review

The quantitative performance criteria which will be used to monitor progress in the implementation of the program are presented in Table 6. In addition to requiring the avoidance of new external arrears and the standard commitments on the exchange and trade system, the program contains five quantitative performance criteria. These are: (a) net credit to the public sector from the Central Bank and the Reserve Bank; (b) net domestic assets of the Central Bank; (c) net foreign assets of the Central Bank; (d) cash reduction in external payments arrears; and (e) disbursements of nonconcessional public sector loans. The stock of net foreign assets of the Central Bank on December 31, 1984 contained deposits which have been pledged as collateral against letters of credit which were unpaid as of that date. It is believed that the amount in question is approximately US$35 million, and the performance criterion on cash reduction in external arrears assumes that these obligations are liquidated by June 30, 1985. As the corresponding liability on the balance sheet of the Central Bank is domestic, the target for the improvement in the net foreign asset position of the Central Bank will be lowered to the extent that such deposits are used to liquidate these letters of credit. Understandings have been reached with the staff that if the amount of the collateral deposits should exceed US$35 million, no adjustment would be made for any such excess.

As a number of key elements--notably, the amount of debt relief and the evolution of the exchange rate--in the program are subject to substantial uncertainties, performance criteria have been set only for June 1985. The remaining criteria will be set at the time of the review with the Fund mentioned in paragraph 30 of the attached letter. Other than the initial purchase, which is equivalent to the full amount of the Dominican Republic's first credit tranche, all subsequent purchases will be subject to the observance of performance criteria and the completion of a review with the Fund. The review with the Fund contemplated in paragraph 30 of the letter of intent will focus in particular on exchange rate policy, interest rate policy, the reduction of external payments arrears, external financing, and the establishment of quantitative performance criteria for September and December 1985. A second review with the Fund, which is expected to take place before February 28, 1986, is also envisaged. This review will assess performance in the period after December 31, 1985, the last test date, and among its objectives will be the evaluation of economic and financial policies for 1986.

Table 6. Dominican Republic: Quantitative Performance Criteria, 1985

	1985		
	June	September	December
Net credit to the public sector (in millions of Dominican pesos)	1,902.0	1,852.0 1/	1,802.0
Net domestic assets of the Central Bank (in millions of Dominican pesos)	1,582.2	1,517.2 1/	1,467.4 1/
Net foreign assets of the Central Bank (in millions of U.S. dollars)	-300.0	-278.6 1/	-227.2 1/
Cash reduction in external arrears (in millions of U.S. dollars) 2/	64.0	74.0 1/	89.0 1/
Disbursements of nonconcessional debt (in millions of U.S. dollars)			
0-1 year (net)			-19.3 3/
1-5 years			64.2
1-12 years			198.5

Source: Technical Memorandum of Understanding.

1/ Indicative ceiling; performance criterion for that date to be set during review with the Fund.

2/ The external arrears referred to here exclude certain potential obligations that could arise from the Monetary Board's Resolution of May 10, 1984 and on which a decision has not been made as yet. No adjustment will be made to the performance criteria as a result of any decision taken in this area.

3/ At no time during 1985 shall the cumulative disbursements exceed US$90.7 million, and there shall be net repayments of US$19.3 million for the year as a whole.

IV. Medium-Term Balance of Payments 1/ and External Debt Scenarios

Prospects for the medium term will be influenced importantly by the degree of commitment to the adjustment process and the level of financial and technical assistance from bilateral and multilateral donors. In this connection, the World Bank has played a supportive role in the preparation of the present program. In view of the importance and complexity of the reform of the electricity tariff structure, a World Bank financial analyst participated directly in various Fund missions where the issue was discussed. Other World Bank staff have assisted the Fund staff in analyzing the Dominican Republic's medium-term prospects.

Moreover, the World Bank is prepared to accelerate two loans held in abeyance pending the adoption of the adjustment policies included in the present program. One, a US$5.8 million Vocational Training loan, is scheduled to be considered by the IBRD Board in May; another, a US$32 million Highways Maintenance loan, may be considered by the Bank's Board the following month. The World Bank will be sending an economic mission to the Dominican Republic during April to examine the country's medium-term prospects, any further policy actions that may be required to improve them, and the possibility of a sector loan, which would assist the economy in 1985-86.

Until the Bank completes this review, it is not in a position to produce policy-oriented medium-term macroeconomic and balance of payments projections. Nevertheless, the staff of the Fund and the Bank concur that the Dominican Republic must undertake a major shift in its external strategy over the medium term. The poor price prospects for sugar and ferronickel, the expected decline and eventual cessation of commercial gold/silver mining, and the recent closure of the bauxite mine underline the need for a strong emphasis on nontraditional raw and processed agricultural exports and tourism. The unification of the foreign exchange market is consistent with this strategy. The World Bank staff also agree on the importance of strengthening both private and public savings, as well as expanding the country's access to concessional loans. The Bank will be emphasizing, in its discussions with the authorities, a lending strategy that would strengthen the management and operations of specific state institutions, both of which have proven to be particularly weak in the recent past. The Bank also plans to assist the authorities in developing a public investment program that could attract stronger support from official lenders. This should permit the Bank and other official lenders to increase their financial support.

The prospects for the balance of payments over the medium term are presented in Table 7. Underlying this scenario is the assumption that the adjustment effort initiated in 1985 will be maintained in the

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1/ The balance of payments scenario presented here does not incorporate assumptions on the interest cost and repayment stream of the exceptional financing needed to cover the balance of payments gaps in 1985-88, given the uncertainties surrounding the conditions attached to such financing.

Table 7. Dominican Republic: Medium-Term Balance of Payments, 1984-90 1/

(In millions of U.S. dollars)

	Prel. 1984	Proj. 1985	1986	1987	1988	1989	1990
Current account	-226	-29	-54	-44	-66	-122	-113
Trade balance	-391	-350	-389	-433	-490	-590	-610
Exports, f.o.b.	(864)	(800)	(842)	(884)	(919)	(917)	(1,003)
Imports, f.o.b.	(-1,255)	(-1,150)	(-1,231)	(-1,317)	(-1,409)	(-1,507)	(-1,613)
Services (net)	-102	6	49	97	125	151	160
Receipts	(534)	(609)	(648)	(690)	(735)	(783)	(833)
Of which: travel	/403/	/478/	/512/	/547/	/586/	/627/	/670/
Payments	(-637)	(-603)	(-599)	(-593)	(-610)	(-632)	(-673)
Of which: interest	/-269/	/-236/	/-207/	/-168/	/-155/	/-154/	/-161/
Transfers (net)	267	315	286	292	299	317	337
Private	(210)	(215)	(226)	(242)	(259)	(277)	(297)
Public	(57)	(100)	(60)	(50)	(40)	(40)	(40)
Capital account	71	-120	-39	27	107	239	309
Direct investment	68	42	60	65	70	76	82
Medium- and long-term loans (net)	16	-143	-99	-38	37	163	227
Drawings	(306)	(280)	(284)	(295)	(316)	(340)	(372)
Amortization	(-290)	(-423)	(-383)	(-333)	(-279)	(-177)	(-145)
Other	-13	-19	--	--	--	--	--
Overall balance	-155	-150	-93	-17	41	117	196
Financing							
Net foreign assets of the Central Bank (- increase)	-92	-109	-116	-99 2/	-94 2/	-117 2/	-196 2/
Of which: IMF	(-10)	(29)	(-22)	(-49)	(-44)	(-64)	(-48)
purchases	/--/	/61/	/17/	/.../	/.../	/.../	/.../
repurchases	/10/	/32/	/39/	/49/	/44/	/64/	/48/
Arrears (- reduction)	247	-77	...	...	...	...	...
Financing gap	--	336	209 3/	116 3/	53 3/	--	--

Sources: Data provided by the Dominican authorities; and Fund staff estimates and projections.

1/ Before debt relief in 1985-90.
2/ Includes increase in gross reserves of a minimum of US$50 million per annum.
3/ Before reduction of external arrears through cash payments.

coming years and, in particular, that fiscal and monetary policies will remain cautious and be supported by appropriate exchange rate policies. On the basis of prospective capital inflows, it is projected that the Dominican Republic would continue to face financing gaps through 1988. Such gaps would necessitate additional financing, including possible further debt relief.

On the export side the prospects for traditional agricultural exports, especially for sugar, are not bright and at best only a very slow growth in receipts is likely. Nontraditional exports are forecast to grow at an annual rate of 19 percent in 1986-90 as a result of the exchange rate action.

Following the substantial decline in import volume in prospect for 1985, it will be necessary to provide for some restocking in 1986 and to allow for a modest expansion in volume to accommodate the expected resumption of economic growth. Over the period 1986-90 it is projected that import payments will rise at a compound rate of 7 percent per annum to reach US$1.6 billion. On this basis the trade deficit will widen considerably, reaching about US$600 million by 1990.

The services account is forecast to record growing surpluses from 1986 to 1990. This is essentially attributable to two factors: first, reflecting the recent adjustments in exchange rate policy, receipts from tourism are expected to expand steadily to reach US$670 million by 1990; and, second, before the impact of new financing and rescheduling to cover the external gaps, interest obligations are expected to decline.

It is projected that the net inflow of unrequited tranfers should rise at an annual rate of some 4 percent between 1986 and 1990 to reach about US$337 million by the latter year. Private transfers are projected to increase at an annual rate of 7 percent per annum from 1986 to 1990 to reach US$300 million. By contrast, public transfers are forecast to decline from the exceptionally high level expected in 1985 and should average US$46 million a year in the period 1986-90.

For 1986 it is likely that the capital account will continue to register an outflow, but of a much smaller magnitude than in 1985. From 1987 to 1990 net public and private capital inflows are projected to increase on account of the expected recovery in investment and economic activity, and lower amortization.

The balance of payments is expected to record overall deficits in 1986 and 1987 but should thereafter shift into surplus. By 1990 it is projected that the overall surplus will approach US$200 million. Over the period 1987-90 it would be important to improve the net foreign asset position of the Central Bank which will be negative at end-1985. Hence, an annual increase in gross reserves of at least US$50 million in 1987-90 is targeted. Financing gaps totaling nearly US$400 million are in prospect, before possible debt relief, in the period 1986-88. To cover these gaps, additional financing would be required. The cost of such financing, under certain working assumptions and as shown in Table 8, would widen the current account deficits between 1985 and 1990 by increasing amounts in every year, reaching some US$137 million in 1990 and resulting in a current account deficit of US$250 million in that year. When allowing for such additional financing, the ratio of the current account deficit to GDP is projected to increase from 1.7 percent in 1985 to 4.2 percent in 1989 and then to decline to 3.9 percent in 1990. At these levels, the ratios would be still below the ones prevailing during 1981-84.

Before debt relief the Dominican Republic, in the short run, faces a very serious debt servicing problem, with scheduled obligations amounting to 64 percent and 49 percent of exports of goods and nonfactor services in 1985 and 1986, respectively. However, in the following years, debt service obligations would decline rapidly, provided external debt policies are prudent, and by 1990 would be around 20 percent of exports of goods and nonfactor services. Similarly, the ratio of outstanding debt to GDP, which is projected to peak at 58 percent at the end of 1985, is forecast to decline in every year thereafter to 42 percent in 1990. Overall, the structure of the medium- and long-term debt is not unfavorable, with the average maturity being 17 years, the average interest rate 7.7 percent, and the average grace period 5 years. Nevertheless, for the immediate future the situation is rendered very difficult by the bunching of relatively short-term obligations and the poor prospects for traditional merchandise exports.

As noted above, the Dominican Republic's external debt profile will worsen if provision is made for the additional financing required to cover the external gaps projected for the period 1985 through 1988. Moreover, the service payments associated with such additional financing are projected to result in external gaps beyond 1988, necessitating further exceptional financing. If account is taken of such financing, the outstanding debt in relation to GDP would peak at 66 percent in 1985 and then decline only gradually to about 60 percent by 1990, compared with 55 percent at the end of 1984. The initial impact of debt relief on the debt service ratio would be positive, leading to a reduction during the period through 1987. Thereafter, however, the debt service ratio, at an average of 33 percent in 1988-90, would be significantly higher than the ratio that would prevail in the absence of debt relief in earlier years. While such debt service could still be considered manageable, it clearly underscores the need for continued strong adjustment over the medium term and for a policy that seeks actively to shift resources to the external sector.

With regard to the 1985 debt relief exercise, the Dominican authorities have already approached the official creditors of the Paris Club. In the case of the commercial banks, formal negotiations have started and it is expected that discussions will be concluded by late April. It is to be noted that all purchases under the requested arrangement, other than the initial purchase, which represents the entire amount of the first credit tranche, are contingent, inter alia, on the conclusion of the debt rescheduling exercise.

Table 8. Dominican Republic: Key External Debt Indicators

	Prel. 1984	Proj. 1985	1986	1987	1988	1989	1990
Debt outstanding (in millions of U.S. dollars; end of period) 1/	2,863	2,652 2/	2,531 2/	2,444 2/	2,437 2/	2,536 2/	2,715 2/
Of which: IMF	(221)	(250)	(228)	(179)	(135)	(71)	(23)
Debt service (in millions of U.S. dollars) 3/	658	898	723	556	485	395	354
Public and private	489	601	527	434	353	226	186
Principal	(290)	(423)	(370)	(310)	(252)	(145)	(112)
Interest (including short-term)	(199)	(178)	(157)	(124)	(101)	(81)	(74)
IMF	28	52	59	66	57	73	52
Repurchases	(10)	(32)	(39)	(49)	(44)	(64)	(48)
Charges	(18)	(20)	(20)	(17)	(13)	(9)	(4)
Other central bank liabilities	151	139	109	9	9	9	9
Principal	(99)	(111)	(94)	(--)	(--)	(--)	(--)
Interest	(52)	(28)	(15)	(9)	(9)	(9)	(9)
Short-term borrowing (net)	-10	19	--	--	--	--	--
Debt contracted after December 31, 1984	--	10	28	47	66	87	107
Principal	(--)	(--)	(13)	(23)	(27)	(32)	(33)
Interest	(--)	(10)	(15)	(24)	(39)	(55)	(74)
Repayment of arrears	--	77	... 4/	... 4/	... 4/	... 4/	... 4/
Debt outstanding/GDP (in percent) 5/	55.0	57.8	51.5	46.5	43.3	42.2	42.2
Debt service/exports of goods and nonfactor services (in percent) 5/	47.2	63.8	48.5	35.3	29.3	23.0	19.3
Debt outstanding/GDP (in percent) 6/	55.0	66.1	65.1	63.1	61.7	61.3	60.3
Debt service/exports of goods and nonfactor services (in percent) 6/	47.2	45.4	37.4	32.0	31.9	34.0	32.5

Sources: Data provided by the Dominican authorities; IBRD, DRS; and Fund staff estimates and projections.

1/ Excluding international reserve liabilities of the Central Bank, other than the IMF.
2/ Before debt that may be contracted in connection with the financing gaps projected for 1985-88.
3/ On the basis of scheduled payments.
4/ Before provision for reduction of arrears that will be outstanding at end-1985.
5/ Excluding the potential impact of the financing gaps in 1985-88.
6/ Including the potential impact of the financing gaps in 1985-88.

V. Staff Appraisal

The Dominican Republic has experienced severe external and internal imbalances in recent years. While adverse external factors contributed to this development, inappropriate demand management and exchange rate policies were major factors. Large overall balance of payments and fiscal deficits were recorded, leading to a virtual exhaustion of liquid foreign exchange reserves and the accumulation of a substantial amount of external payments arrears. Pricing policies gave rise to serious distortions in the allocation of resources and fostered excessive levels of consumption.

The Government which took office on August 16, 1982 adopted a medium-term economic program which was supported by an extended arrangement from the Fund, approved by the Executive Board on January 21, 1983. This program was aimed at achieving a viable external payments position in the context of a satisfactory rate of economic growth. However, implementation of the program did not produce the degree of adjustment that had been sought. The overall balance of payments deficit remained virtually unchanged in 1983 and the deficit of the nonfinancial public sector was significantly larger than programmed. The lack of major adjustment in the first year of the program, subsequent delays in formulating a program for 1984, and uncertainty about the timely implementation of adjustment measures led to heavy pressures on the peso in the parallel market. Thus, the premium of the U.S. dollar in that market doubled in the early months of 1984.

In formulating the financial program for 1985, the main priority was to initiate action which would result in a rapid improvement in both the internal and external financial positions and thereby facilitate the mobilization of the external and domestic resources to sustain an adequate level of economic growth.

A major feature of the program was the reform of the exchange system. In late January 1985 the exchange system was unified and since then the peso has been floating freely with the exchange rate being determined by market forces. This action has paved the way for the restoration of realistic cost/price relationships which would permit an adequate level of producer incentives and would eliminate the need for budgetary subsidies. The staff welcomes the adoption of this exchange rate policy.

To complement the action taken in the exchange rate area the program calls for restrained fiscal and monetary policies. Thus, a reduction in the ratio of the fiscal deficit to GDP is targeted. However, the exchange rate action has resulted in a significant increase in outlays of the public sector as previously implicit costs have now become explicit. In order to deal with this situation while ensuring that the overall deficit is contained to manageable proportions, it has been necessary to introduce temporary taxes on receipts from most exports of goods and services. It is intended that this measure, which gives rise to multiple currency practices subject to Fund approval, will be replaced by permanent fiscal measures as soon as possible. The staff considers that these exchange taxes should be re-examined at an early stage and the mid-term review will focus on the identification of appropriate alternative revenue sources.

Particular vigilance will be required in the area of expenditure control in 1985 if the fiscal targets in the program are to be attained. In this connection it will be vital that a policy of wage restraint be effectively implemented and therefore the authorities' decision not to increase wages unless compensating measures are taken is particularly welcome.

A crucial element in the program is the reform of the pricing structure of the principal public enterprises. The actions taken in this area, which include substantial increases in electricity tariffs and food prices, will contribute importantly to the reduction of the fiscal deficit in the current year and to the strengthening the financial position of the public enterprises over the medium term. Further adjustments should be made on a timely basis if conditions indicate they are needed.

As the public sector will have no recourse to domestic bank credit on a net basis during 1985, the authorities will be in a position to pursue a very cautious credit policy, thus facilitating the attainment of the program's balance of payments objectives. A number of measures have been taken to strengthen central bank control over the liquidity of the financial system and to promote the growth of financial savings. The staff welcomes the increases in interest rates on financial certificates and the reduction in their minimum denominations as an important first step toward a more flexible interest rate policy.

The policies contained in the program are expected to bring about a major improvement in the external accounts, with the current account deficit (before rescheduling) being reduced significantly. Moreover, the medium-term prospects appear manageable provided the adjustment effort is sustained and continued exceptional financial assistance is forthcoming. Given the extremely heavy debt service burden, there is need for caution in further borrowing, and for this reason the program places strict limits on disbursements of nonconcessional loans. Notwithstanding the adjustment effort being undertaken, it will not be possible to service fully the external debt obligations falling due in 1985. Accordingly, it is important that early agreement be reached on the rescheduling of obligations with both official creditors and the commercial banks.

The staff has been assured that the taxes levied on the domestic currency proceeds of exports, which give rise to multiple currency practices, have been introduced on a temporary basis. The authorities intend to replace these taxes as soon as possible with appropriate alternative fiscal measures. The staff also welcomes the intention of the Central Bank not to intervene in the foreign exchange market to influence the exchange rate. In these circumstances, the staff recommends that the Executive Board approve the exchange restrictions and multiple currency practices retained by the Dominican Republic.

Overall, the staff believes that the program for 1985 lays the groundwork for the resumption of economic growth in the context of financial stability both internally and externally. Nevertheless, given the magnitude of existing imbalances, the adjustment effort will have to be sustained for a number of years. In this connection it will be important that the authorities be ready to ensure that additional corrective actions are taken in a timely manner. In view of the measures already adopted and those which are being implemented, the staff believes that the program for which the Dominican Republic authorities have requested assistance in the form of a stand-by arrangement in an amount equivalent to SDR 78.5 million, is deserving of Fund support. The implied annual access of 70 percent of quota proposed under the arrangement is justified by the Dominican Republic's balance of payments need and by the strength of its adjustment efforts.

VI. Proposed Decisions

The following draft decisions are proposed for adoption by the Executive Board.

I. Approval of Exchange Restrictions and Multiple Currency Practices

The Dominican Republic retains restrictions on payments and transfers for current international transactions and multiple currency practices as described in EBS/85/76. In light of the implementation by the Dominican Republic of policies for balance of payments adjustment, which are supported by a stand-by arrangement (EBS/85/75), the Fund grants approval for the retention of these restrictions and multiple currency practices until the conclusion of the 1985 Article IV consultation, or August 15, 1985, whichever is earlier.

II. Stand-By Arrangement

1. The Government of the Dominican Republic has requested a stand-by arrangement for the period April __, 1985-April __ , 1986 for an amount equivalent to SDR 78.5 million.

2. The Fund approves the stand-by arrangement attached to EBS/85/75, and waives the limitation in Article V, Section 3 (b)(iii).

Dominican Republic - Fund Relations
(As of February 28, 1985)

I. Membership Status

(a) Date of membership: December 28, 1945
(b) Status: Article VIII

A. Financial Relations

II. General Department (General Resources Account)

		Millions of SDRs	Percent of Quota
(a)	Quota:	112.10	
(b)	Fund holdings of Dominican pesos:	337.80	301.33
(c)	Fund credit:	225.70	201.34
	Of which: CFF	78.75	70.25
	Buffer stock	23.19	20.69
	Credit tranche	0.00	0.00
	EFF	61.88	55.20
	Enlarged access under EFF	61.88	55.20
(d)	Reserve tranche position:	--	--
(e)	Current Operational Budget:	--	--
(f)	Lending to the Fund:	--	--

III. Current Stand-By or Extended Arrangement and Special Facilities

(a) Extended arrangement

(i) Duration: From January 21, 1983 to January 20, 1986 but canceled on January 17, 1985
(ii) Amount: SDR 371.25 million
(iii) Utilization: SDR 123.75 million

(b) Special facilities since 1974:

Facility	Date of purchase	Amount
BSFF	August 1983	SDR 12.64 million
CFF	January 1983	SDR 42.75 million
BSFF	July 1982	SDR 10.55 million
CFF	May 1982	SDR 36.00 million
CFF	September 1979	SDR 27.50 million
CFF	January 1979	SDR 6.00 million
BSFF	January 1979	SDR 11.51 million
CFF	September 1976	SDR 21.50 million

IV. SDR Department

(a)	Net cumulative allocation:	SDR 31.59 million
(b)	Holdings:	SDR 0.25 million (0.79 percent of net cumulative allocation)
(c)	Current designation plan:	Not in designation plan

B. Nonfinancial Relations

V. Exchange Rate Arrangement

Since January 23, 1985 the Dominican peso has been floating freely. Prior to that date it was linked to the U.S. dollar at the rate of RD$1=US$1. An active parallel market existed and a number of multiple currency practices were in operation.

Exchange taxes of 36 percent and 5 percent, respectively, are levied on traditional and nontraditional exports. These taxes constitute multiple currency practices subject to Fund approval. The exchange restrictions and the multiple currency practices of the Dominican Republic have not been approved by the Fund.

VI. Last Article IV Consultation

The last Article IV consultation was concluded by the Executive Board on August 8, 1984 (EBM/84/124). The relevant staff reports were SM/84/161 and SM/84/166. For consultation purposes, the Dominican Republic is on the 12-month cycle.

VII. Technical Assistance

The Bureau of Statistics provided technical assistance in June 1984 in the field of government finance statistics, with special reference to (1) the reconciliation of fiscal data compiled by the Ministry of Finance and the Central Bank; (2) the compilation of data on central government financing and debt; and (3) the compilation of data on the fiscal operations of the local governments.

VIII. Resident Representative

A resident representative is expected to be stationed in Santo Domingo in early April.

Dominican Republic--Basic Data

Area and population	
Area	48,400 sq. kilometers
Population (mid-1984)	6.3 million
Annual rate of population increase (1980-84)	2.9 percent
GDP (1984) 1/	SDR 5.1 billion
GDP per capita (1984) 1/	US$826

	1981	1982	1983	Prel. 1984
Origin of GDP		(percent)		
Agriculture and fishing	16.9	17.2	17.2	...
Mining and manufacturing	22.4	21.8	22.2	...
Construction	6.6	6.2	6.8	...
Commerce, transportation, and communications	24.4	25.0	24.3	...
Government	9.9	10.3	10.0	...
Other	19.8	19.5	19.5	...
Ratios to GDP 2/				
Exports of goods and services	21.1	14.6	17.6	26.9
Imports of goods and services	29.4	22.8	24.7	36.3
Current account of the balance of payments 3/	-5.6	-5.6	-6.0	-4.3
Central government revenue	12.8	9.6	11.2	15.0
Central government expenditure	15.0	12.4	13.9	20.7
Central government savings	2.1	-0.4	1.1	-1.1
Public sector overall deficit	-6.2	-6.2	-5.6	-7.5
External debt (end of year) 4/	25.7	26.1	38.1	55.0
Gross national savings	18.7	15.2	15.4	16.2
Gross domestic investment	24.3	20.8	21.4	20.5
Money and quasi-money (end of year) 5/	16.3	17.3	16.8	18.0
Annual changes in selected economic indicators 6/				
Real GDP per capita	1.2	-1.3	1.0	-1.8
Real GDP	4.1	1.6	3.9	1.0
GDP at current market prices	9.1	9.0	11.4	18.7
Domestic expenditure (at current prices)	3.6	9.8	13.9	15.4
Investment	(3.3)	(-6.9)	(16.8)	(5.2)
Consumption	(3.6)	(14.9)	(13.2)	(18.0)
GDP deflator	4.8	7.3	7.2	17.5
Cost of living index (annual averages)	7.5	7.6	6.9	24.4
Central government revenue	4.0	-18.5	22.3	19.6
Central government expenditure	0.3	-10.0	17.4	12.7
Money and quasi-money 5/	11.9	15.4	7.8	28.0
Money	(12.8)	(11.5)	(7.2)	(46.8)
Quasi-money	(10.9)	(19.8)	(8.5)	(8.4)
Domestic credit 7/	28.2	45.4	34.5	30.2
Credit to public sector (net)	(32.5)	(32.5)	(23.2)	(8.7)
Credit to private sector	(-2.3)	(8.0)	(6.6)	(10.5)
Exports, f.o.b. (in U.S. dollars)	23.5	-35.4	2.3	10.0
Imports, f.o.b. (in U.S. dollars)	-4.5	-13.4	2.0	-2.1

	1981	1982	1983	Prel. 1984
Central government finances	(millions of Dominican pesos)			
Revenue	926.0	754.6	923.2	1,103.9
Expenditure	1,080.9	972.9	1,142.3	1,287.2
Overall deficit	-154.9	-218.3	-219.1	-183.3
External financing (net)	60.2	48.4	81.3	139.7
Domestic financing (net)	94.7	169.9	137.8	43.6
Balance of payments	(millions of U.S. dollars)			
Exports, f.o.b.	1,188.0	767.6	785.2	863.9
Imports, f.o.b.	-1,451.7	-1,257.3	-1,282.2	-1,255.0
Interest payments	-304.9	-285.5	-304.0	-268.5
Travel income	206.3	266.1	320.0	402.9
Other services and transfers (net)	-43.6	67.0	59.9	30.6
Balance on current account	-405.9	-442.0	-421.1	-226.1
Direct investment	79.7	-1.4	22.0	68.5
Medium and long-term loans (net)	153.6	150.5	24.1	16.0
Other 8/	63.0	-63.4	22.3	-13.1
Overall balance	-109.6	-356.3	-352.7	-154.7
Extraordinary financing	--	--	294.5	246.9
Change in net foreign assets (increase -)	109.6	356.3	58.2	-92.2

	December 31			
International reserve position	1981	1982	1983	1984
	(millions of SDRs)			
Central Bank (gross)	243.6	156.3	195.1	273.4
Central Bank (net)	-276.9	-615.2	-408.9	-342.7
Rest of banking system (net)	-59.1	-20.1	-40.9	-27.1

1/ Calculated at the rate of RD$2 per U.S. dollar.

2/ GDP in terms of U.S. dollars where prior to 1983 foreign transactions were at the rate of RD$1 per U.S. dollar, in 1983 at the rate of RD$1.3 per U.S. dollar, and in 1984 at the rate of RD$2 per U.S. dollar.

3/ Includes public and private transfers.

4/ Debt of all maturities, including use of Fund credit, but excluding other foreign reserve liabilities.

5/ Includes only banking system liabilities.

6/ Data are in terms of Dominican pesos unless otherwise specified.

7/ Changes in relation to broad money at the beginning of the period.

8/ Includes SDR allocation in 1981, short-term public and private capital (net), gold revaluation and monetization, and errors and omissions (net).

Dominican Republic: Relations with the World Bank Group

(In millions of U.S. dollars)

A. IBRD Operations (as of January 31, 1985)

	Commitments (net of cancellations)	Disbursements	Undisbursed Amount
Agriculture and irrigation	69.0	33.6	35.4
Industry	25.0	25.0	--
Tourism	46.0	35.9	10.1
Transport	65.0	64.5	0.5
Population	5.0	5.0	--
Education	12.0	12.0	--
Housing	25.4	2.4	23.0
Sugar rehabilitation	35.0	3.6	31.4
Urgent imports requirements	25.0	25.0	--
Energy	3.8 1/	--	3.8
Total	311.2	207.0	104.2

B. IFC Operations (as of February 28, 1985)

	Loans	Equity	Total
Commitments	16.0	2.9	18.9
Total held by IFC	8.6	2.9	11.5
Total undisbursed	4.9	0.4	5.3

C. IBRD Loan Transactions

	Actual				
	1980	1981	1982	1983	1984
Disbursements	39.1	33.8	24.9	26.9	21.1
Repayments	2.1	2.3	2.3	4.0	10.5
Net lending	37.0	31.5	22.6	22.9	10.6

Source: IBRD.

1/ Not yet effective.

Dominican Republic: Summary of Financial Program for 1985

1. Principal targets

Nonquantitative:

a. To initiate the process of returning to a viable external and internal financial situation while paving the way for a resumption of a satisfactory rate of economic growth.

b. To restore confidence externally and internally and thus facilitate the mobilization of the resources required to finance both curent operations and investment activities.

Quantitative:

a. To reduce the ratio of the deficit of the current account of the balance of payments to GDP (before rescheduling) to 0.6 percent from 4.3 percent in 1984, and to achieve an increase in the net international reserves of US$109 million.

b. To reduce the ratio of the consolidated fiscal deficit to GDP to 4.9 percent in 1985 from 7.5 percent in 1984. This deficit will be fully covered by foreign financing.

c. To contain the rate of inflation in 1985 to about 24 percent on an average annual basis.

2. Main assumptions

a. Nominal GDP is projected to rise by 23 percent in local currency terms in 1985 while real GDP will rise by 2 percent.

b. Export prices in U.S. dollar terms are projected to decline by almost 8 percent while import prices in U.S. dollar terms are forecast to rise by 1 percent. Thus, the terms of trade are expected to deteriorate by about 8 1/2 percent.

c. Interest rates in international markets, on average in 1985, are forecast to be 2 percentage points lower than in 1984.

d. World oil prices will not exceed US$28/barrel on average in 1985.

e. Debt relief is provided by June 30, 1985.

3. Principal elements and instruments

a. Fiscal policy

A key element of the program is a major improvement in the public finances. The principal revenue measure taken is the imposition of taxes on traditional and nontraditional exports of goods and services at rates of 36 percent and 5 percent, respectively. This measure will generate RD$712 million, or about one third of total central government revenue in 1985. Substantial new revenue will be raised from increases in the prices of petroleum products. On the expenditure side, both current and capital outlays are being tightly controlled and it is explicitly provided that no salary increase will be granted unless Congress approves compensating revenue or expenditure measures.

b. Public enterprises

The program calls for fundamental reforms in the public enterprise sector aimed at restoring financial viability in the medium term. Thus, a major tariff reform has been undertaken in the case of the Electricity Corporation (CDE), which should eliminate losses by 1987. Similarly, corrective actions have been instituted in the case of the Price Stabilization Institute (INESPRE) and the State Sugar Company (CEA).

c. Pricing policy

An integral element of the program is the restoration of realistic cost/price relationships in the economy. To this end, a number of price increases have been effected. These relate to foodstuff products sold by INESPRE, petroleum products, and other goods and services subject to price control. Since January 23, 1985, petroleum products are being sold at prices that fully reflect the import cost. In the event that further action is warranted in this area, appropriate measures will be discussed with the authorities.

d. Monetary and credit policies

In order to slow the growth of domestic liquidity, the program provides that there will be no net expansion of banking system credit to the public sector during 1985 and a sizable contraction in the net domestic assets of the Central Bank is targeted. This restrictive policy will contribute importantly to slowing inflationary pressures and improving the balance of payments. To foster the mobilization of domestic savings, interest rate on financial certificates have been adjusted upward and minimum denominations have been reduced. Moreover, certain lending rates have been increased with a view to improving the allocation of resources.

e. External sector policies

In the external sector the major action is the unification of the exchange system and the adoption of a freely floating exchange rate system. The Central Bank has indicated its intention not to intervene in the foreign exchange market. As the Dominican Republic faces a very serious debt problem, the program places strict limits on disbursements of nonconcessional public sector or government guaranteed loans. Moreover, the program is predicated on debt relief being secured by end-June 1985. At end-1985 external arrears will have been reduced by nearly 80 percent, of which about one quarter will be through cash payments.

Dominican Republic: Operations of the Principal Public Enterprises

The four principal public sector enterprises, the Dominican Electricity Corporation (CDE), the Price Stabilization Institute (INESPRE), the State Sugar Company (CEA) and the Corporation of State Enterprises (CORDE), improved their financial position significantly in 1984. Their combined current account shifted from a deficit of almost RD$150 million in 1983 to a surplus of RD$77 million in 1984 and, despite stepped-up investment spending, the consolidated overall deficit declined from RD$176 million to RD$77 million. The improved financial position of these enterprises reflected the impact of the exchange incentive--introduced in April 1984--on sugar revenues, increased operating efficiency--especially in CORDE, and CDE--and the April 1984 domestic price increases of sugar and imported food products intermediated by INESPRE.

On January 23, 1985 additional price action was taken. However, the unification of the exchange markets has resulted in a sharp increase in debt service, in local currency terms. Consequently, a portion of the exchange tax on export receipts will be used to help meet the external obligations of the public enterprises. The current account surplus of these enterprises is projected to amount to RD$100 million. Investment spending is projected to more than triple, in part due to the effect of the exchange rate unification which has substantially raised the cost of imported inputs in local currency terms. Moreover, the execution of CDE's investment plan for 1985 is projected to raise investment in real terms. The overall deficit of the enterprises is projected to reach RD$344 million.

1. CDE

The operations of the CDE have been adversely affected in recent years by inadequate maintenance and obsolete equipment resulting in low fuel efficiency in electricity generation and in energy losses during transmission. Moreover, there has been widespread use of illegal connections and the rest of the public sector did not pay for its electricity usage. Since mid-1983, steps have been taken to tackle these problems: an investment program, which included the installation of new transmission facilities and the refurbishing of generators, was initiated; and revenue collection efforts were intensified. A program to curtail the illegal use of electricity has reduced losses from an average of 36 percent of energy generated in 1983 to only 27 percent by September 1984 and is scheduled to further reduce losses in 1985. Electricity tariffs have been raised to offset operating losses and a further revision in the tariff structure is being implemented with technical assistance provided by the IBRD. Finally, all public sector entities are being required to pay their electricity bills.

Operating costs of CDE are scheduled to increase significantly in 1985, reflecting mainly the impact of the exchange rate unification on the CDE's fuel import bill. For the long term, alternative energy sources are being developed. In 1984, the first coal-fired generating plant was completed and a second is scheduled to become operational in 1985. Coal is to be imported under a long-term contract from Colombia, initially at prices below prevailing world market prices. In addition, in 1985 a new reservoir is expected to be filled and once the capital equipment has been put in place additional hydropower will be available, further reducing the dependence of the Dominican Republic on imported petroleum.

2. INESPRE

Significant cost/price distortions have arisen in recent years with INESPRE's policy of importing foodstuffs for domestic sale at subsidized prices. Prior to 1984, however, the magnitude of the subsidy was disguised as imports were accounted for at the official exchange rate. In April 1984, the transfer of import payments to the parallel market raised INESPRE's outlays on goods and services in local currency terms by over 50 percent and consumer prices of a number of basic foodstuffs were increased. In an effort to cushion the impact of these increases on the lowest income group, stores were established in the poorest neighborhoods under the "Popular Sales" program. Imported foodstuffs were sold at prices lower than in regular stores; the operating cost of this program in 1984 amounted to RD$14 million. INESPRE's overall deficit rose from RD$13 million in 1983 to RD$22 million in 1984, and unlike previous years when external financing in the form of commodity credit had been available, almost all of the deficit was financed by recourse to domestic bank borrowing.

In 1985, the full impact of the exchange rate measures on import costs and on interest payments will be felt. In January 1985 prices of imported and domestically produced food, intermediated by INESPRE, were raised. Milk prices rose by 36 percent to RD$0.75 per quart. Prices for soybean oil and rice were raised by 37 percent and 41 percent, respectively, and for noodles, a staple in low income diets, by 15 percent.

Flour prices were not adjusted; however, the increased import cost has not been passed on to INESPRE and the wheat subsidy is in the form of a cash payment from the Central Government to the flour company. The popular sales program has continued but its operations have been rationalized and it is estimated that the cost of this program will not exceed RD$11 million in 1985. Despite these measures, INESPRE will continue to face financial difficulties in 1985 and the overall deficit is projected to reach RD$67 million, primarily because previously implicit subsidies are now explicit.

3. CEA

The CEA accounts for about one half of the Dominican Republic's sugar exports and all of domestic sugar sales. In 1984 the financial position of the CEA improved significantly and the company recorded a small overall surplus of RD$6 million compared with overall deficits averaging RD$80 million in the three preceding years. This significant improvement in CEA's financial position reflected the introduction, in April 1984, of the exchange incentive which valued sugar exports at RD$1.48 per U.S. dollar and a 20 percent increase in the domestic sale price of sugar.

With the unification of the exchange markets in January 1985, export earnings will be valued at the free market rate (estimated at RD$2.8 per U.S. dollar) although subject to an exchange tax of 36 percent. However, world free market sugar prices are projected to remain depressed during 1985 and the proportion of sales at preferential prices is expected to fall given the recent extension of the current U.S. quota on sugar imports from 12 months to 14 months. These two factors are projected to virtually offset the windfall gain from the exchange rate action. In January the domestic price of refined sugar was increased by 36 percent to RD$0.42 per pound (equivalent to US$0.13 per pound compared with a prevailing free market world price of around US$0.04 per pound). Higher operating costs due to increased fuel prices and to the impact of the exchange rate adjustment on interest payments are to be partly compensated for by transfers from the Central Government. Efforts are to continue in 1985 to refurbish inefficient mills and to improve the transportation system in order to reduce operating costs in the long run. The CEA is expected to show a small overall surplus in 1985.

4. CORDE

This group of companies underwent a major restructuring in 1984. At that time, the workforce was reduced, sale prices were raised to reflect costs, and efficient operating procedures were implemented. As a result, the overall deficit of US$8 million recorded in 1983 was eliminated and there was a small surplus of US$1 million.

These efforts are expected to be sustained in 1985 and an overall surplus of US$2.5 million is projected.

Table 9. Dominican Republic: Operations of the Principal Public Enterprises, 1981-85

(In millions of Dominican pesos)

	1981	1982	1983	Prel. 1984	Proj. 1985 1/
I. Consolidated Operations of the Principal Public Enterprises					
Total revenue	788.1	741.1	775.1	1,223.8	1,612.7
Operating revenue	780.8	710.8	773.5	1,222.2	1,609.8
Capital	7.3	30.3	1.6	1.6	2.9
Total expenditure	1,009.0	968.4	1,011.6	1,291.8	2,357.0
Operating expenditure	844.0	767.9	847.9	1,078.4	1,610.9
Wages and salaries	(167.6)	(174.3)	(183.6)	(218.4)	(248.5)
Goods and services	(662.6)	(587.2)	(662.9)	(855.8)	(1,362.3)
Other	(13.8)	(6.4)	(1.4)	(4.2)	(0.1)
Interest payments	50.9	71.9	82.4	53.2	168.4
Capital	114.1	128.6	81.3	160.2	577.7
Capital formation	(81.8)	(123.2)	(68.9)	(138.9)	(571.2)
Other	(32.3)	(5.4)	(12.4)	(21.3)	(6.5)
Transfers (net)	22.8	28.8	60.8	-8.9	400.2
Current	1.2	16.6	8.0	-13.7	270.4
Capital	21.6	12.2	52.8	4.8	129.8
Current account surplus or deficit (-)	-112.9	-112.4	-148.8	76.9	100.9
Overall deficit	-198.1	-198.5	-175.7	-76.9	-344.1
Memorandum item					
Operating surplus or deficit (-)	-63.2	-57.1	-74.4	143.8	-1.1

Table 9. Dominican Republic: Operations of the Principal Public Enterprises, 1981-85 (Continued)

(In millions of Dominican pesos)

	1981	1982	1983	Prel. 1984	Proj. 1985 1/
II. Dominican Electricity Corporation (CDE)					
Current revenue	173.6	216.9	223.2	291.1	620.2
Own revenues	172.8	198.5	215.2	291.1	441.5
Transfers from Central Government	0.8	18.4	8.0	--	178.7
Current expenditure	218.5	229.9	293.5	307.9	554.8
Wages and salaries	36.3	41.1	50.4	55.5	61.2
Goods and services	153.2	162.3	193.0	224.2	458.0
Interest payments	23.5	24.6	50.1 2/	26.8	35.6
Other	5.5	1.9	--	1.4	--
Current account surplus or deficit (-)	-44.9	-13.0	-70.3	-16.8	65.4
Capital revenue	24.9	31.4	46.8	4.5	101.8
Transfers from Central Government	21.6	12.2	46.8	4.5	101.8
Other	3.3	19.2	--	--	--
Capital expenditure	60.6	92.6	52.7	49.7	450.0
Capital formation	60.4	92.6	52.7	45.7	450.0
Purchase of buildings	0.1	--	--	1.9	--
Financial investment	0.1	--	--	2.1	--
Overall deficit	-80.6	-74.2	-76.2	-62.0	-282.8
III. Price Stabilization Institute (INESPRE)					
Current revenue	311.0	309.8	330.0	513.4	771.3
Own revenues	311.0	309.8	330.0	513.4	751.3
Transfers from Central Government	--	--	--	--	20.0
Current expenditure	366.7	322.7	339.6	519.0	815.0
Wages and salaries	15.4	16.0	18.6	20.3	21.7
Goods and services	338.0	289.8	311.9	476.8	713.7
Interest payments	11.8	14.1	9.1	7.8	79.6
Transfers to Central Government	--	--	--	14.1	--
Other	1.5	2.8	--	--	--
Current account surplus or deficit (-)	-55.7	-12.9	-9.6	-5.6	-43.7
Capital revenue	--	9.3	--	--	--
Capital expenditure	3.3	17.5	3.2	16.3	22.9
Capital formation	3.1	17.5	3.2	15.6	22.9
Purchase of buildings	0.2	--	--	0.7	--
Overall deficit (-)	-59.0	-21.1	-12.8	-21.9	-66.6

Table 9. Dominican Republic: Operations of the Principal Public Enterprises, 1981-85 (Continued)

(In millions of Dominican pesos)

	1981	1982	1983	Prel. 1984	Proj. 1985 1/
IV. State Sugar Company (CEA)					
Current revenue	295.1	198.6	225.6	401.2 3/	477.8
Own revenues	295.1	198.6	225.6	401.2 3/	405.5
Transfers from Central Government	--	--	--	--	72.3
Current expenditure	307.3	286.2	294.3	316.6	405.2
Wages and salaries	114.1	115.5	113.0	140.8	163.3
Goods and services	171.1	134.6	157.3	153.9	189.2
Interest payments	15.3	32.7	22.6	18.5	52.1
Transfers to Central Government	--	1.8	--	0.6	0.6
Other	6.8	1.6	1.4	2.8	--
Current account surplus or deficit (-)	-12.2	-87.6	-68.7	84.6	72.6
Capital revenue	--	--	2.8	0.3	28.0
Transfers from Central Government	--	--	2.8	0.3	28.0
Capital expenditure	43.4	13.1	13.0	78.6	97.8
Capital formation	18.3	13.1	13.0	77.4	97.8
Purchase of buildings	--	--	--	--	--
Financial investment	25.0	--	--	1.2	--
Other	0.1	--	--	--	--
Overall surplus or deficit (-)	-55.6	-100.7	-78.9	6.3	2.8

Table 9. Dominican Republic: Operations of the Principal Public Enterprises, 1981-85 (Concluded)

(In millions of Dominican pesos)

	1981	1982	1983	Prel. 1984	Proj. 1985 1/
V. Corporation of State Enterprises (CORDE) 4/					
Current revenue	2.3	3.9	2.7	17.5	11.5
Own revenues	1.9	3.9	2.7	16.5	11.5
Transfers from Central Government	0.4	--	--	1.0	--
Current expenditure	2.4	2.8	2.9	2.8	4.9
Wages and salaries	1.8	1.7	1.6	1.8	2.3
Goods and services	0.3	0.5	0.7	0.9	1.4
Interest payments	0.3	0.5	0.6	0.1	1.1
Other	--	0.1	--	--	0.1
Current account surplus or deficit (-)	-0.1	1.1	-0.2	14.7	6.6
Capital revenue	4.0	1.8	4.8	1.6	2.9
Transfers from Central Government	--	--	3.2	--	--
Other	4.0	1.8	1.6	1.6	2.9
Capital expenditure	6.8	5.4	12.4	15.6	7.0
Capital formation	--	--	--	0.2	0.5
Financial investment	6.8	5.4	12.4	15.4	6.5
Overall surplus or deficit (-)	-2.9	-2.5	-7.8	0.7	2.5

Sources: Data provided by the Dominican authorities; and Fund staff estimates and projections.

1/ Assumes exchange rate of RD$2.8 per U.S. dollar.
2/ Includes interest in arrears to foreign creditors as of December 31, 1983.
3/ Includes RD$113.5 million of exchange incentives and advance export sales.
4/ Holding company for a group of enterprises in which the Government is a majority shareholder.

Table 10. Dominican Republic: Retail Prices of Selected Goods

(In Dominican pesos)

	Unit	March 1984	April 1984	January 1985
Soybean oil	15 pounds	11.90	22.00	30.12 1/
Sugar	1 pound	0.26	0.31	0.42
Rice	1 pound	0.32	0.32	0.45 1/
Flour	1 pound	0.21	0.38	0.38
Noodles	1 pound	0.40	0.48	0.55 1/
Milk	1 quart	0.45	0.55	0.75 2/

Source: Central Bank of the Dominican Republic.

1/ As revised on February 13, 1985.
2/ Price adjusted in late 1984.

Table 11. Dominican Republic: Retail Prices of Selected Petroleum Derivatives, January 1981-January 1985

	1981 January	1983 April	1984 August	1985 January
	(In Dominican pesos per gallon)			
Gasoline	2.57	2.30	2.95	3.95
Diesel	1.15	1.15	2.25	3.95
Kerosene	0.97	0.97	2.00	3.75
LP gas	1.05	1.05	1.28	1.95
Fuel oil	0.65	0.65	2.00	3.80
	(Percentage change from previous level)			
Gasoline	7.5	-10.5	28.3	33.9
Diesel	18.6	--	95.7	75.6
Kerosene	12.8	--	106.2	87.5
LP gas	16.7	--	19.0	56.0
Fuel oil	38.3	--	207.7	90.0

Sources: Ministry of Commerce and Industry; and Central Bank of the Dominican Republic.

Table 12. Dominican Republic: Consumer Prices, 1981-84

	General Index	Food, Beverages, and Tobacco	Housing	Clothes, Shoes, and Accessories	Other
I. Consumer Price Index by Group of Goods					
(May 1976-April 1977 = 100)					
Weights	100.0	51.7	23.9	6.0	18.4
Annual average					
1981	146.8	140.3	156.0	144.8	153.8
1982	158.0	151.4	170.6	158.8	159.8
1983	169.0	161.2	184.7	181.7	167.6
1984 (est.)	210.3	...	...	...	...
End of period					
1981	153.5	145.5	168.8	150.6	157.0
1982	164.5	159.4	176.7	168.1	161.6
1983	177.1	165.7	198.4	202.7	173.3
1984 (est.)	245.0	...	...	...	...
1984					
March	185.8	170.0	212.0	227.3	182.9
June	207.0	194.2	222.3	254.2	201.1
September	224.6	209.4	236.1	288.5	232.1
December (est.)	245.0	...	...	...	...
II. Percentage changes over 12 Months					
Annual average					
1981	7.5	0.4	22.1	8.1	10.0
1982	7.6	7.9	9.3	9.7	3.6
1983	6.9	6.5	8.3	14.4	4.9
1984 (est.)	24.4	...	...	...	...
End of period					
1981	7.3	3.1	18.6	5.9	5.1
1982	7.2	9.6	4.7	11.6	2.9
1983	7.7	4.0	12.3	10.6	7.2
1984 (est.)	38.3	...	...	...	...
1984					
March	12.6	8.1	18.1	32.8	10.2
June	24.4	22.3	21.0	43.2	26.4
September	32.8	29.7	29.4	56.1	38.2
December (est.)	38.3	...	...	...	...

Source: Data provided by the Central Bank of the Dominican Republic.

Table 13. Dominican Republic: Operations of the Central Government, 1981-85

(In millions of Dominican pesos)

	1981	1982	1983	Prel. 1984	Proj. 1985 1/
Total revenue	926.0	754.6	923.2	1,103.9	2,154.0
Current revenue	909.2	745.1	917.4	1,097.6	2,147.5
Tax revenue	734.4	661.3	782.5	1,018.5	2,030.8
Taxes on income and profits	(186.2)	(181.4)	(199.6)	(225.3)	(243.9)
Taxes on property	(7.1)	(8.7)	(9.6)	(25.5)	(27.3)
Taxes on goods and services	(256.4)	(273.9)	(322.3)	(460.3)	(638.5)
Taxes on international trade	(270.8)	(185.2)	(237.7)	(261.3)	(338.6)
Export surcharge	(--)	(--)	(--)	(--)	(712.0)
Other taxes	(13.9)	(12.1)	(13.3)	(46.1)	(70.5)
Nontax revenue	174.8	83.8	134.9	79.1	116.7
Capital revenue	16.8	9.5	5.8	6.3	6.5
Total expenditure	1,080.9	972.9	1,142.3	1,287.2	2,403.6
Current expenditure	756.2	778.5	871.5	1,026.6	1,851.4
Wages and salaries	402.2	427.8	452.1	516.0	482.2
Goods and services	138.7	135.0	162.9	193.9	209.1
Transfers	166.7	164.1	190.1	251.5	789.1
Interest payments	45.9	48.3	62.5	65.2	371.0
Of which: to the Central Bank	(--)	(--)	(--)	(--)	(105.2)
Other	2.7	3.3	3.9	--	--
Capital expenditure	324.7	194.4	270.8	260.6	552.2
Capital formation	151.8	110.7	130.7	156.0	401.8
Capital transfers to nonfinancial public sector	163.0	80.3	114.1	100.0	150.4
Other	9.9	3.4	26.0	4.6	--
Current account surplus or deficit (-)	153.0	-33.4	45.9	71.0	296.1
Overall deficit	-154.9	-218.3	-219.1	-183.3	-249.6
Financing	154.9	218.3	219.1	183.3	249.6
External financing (net)	60.2	48.4	81.3	139.7	...
Drawings	75.8	91.1	138.3	189.7	...
Amortization	-15.6	-42.7	-57.0	-50.0	...
Domestic financing (net)	94.7	169.9	137.8	43.6	...
Central Bank	118.2	195.9	184.1	19.3	...
Reserve Bank	13.9	3.4	-35.7	42.1	...
Private commercial banks	0.5	-1.7	2.1	4.1	...
Other	-37.9	-27.7	-12.7	-21.9	...

Sources: National Budget Office; Central Bank of the Dominican Republic; Ministry of Finance; and Fund staff estimates and projections.

1/ On the basis of an exchange rate of RD$2.8 per U.S. dollar.

Table 14. Dominican Republic: Summary Accounts of the Banking System, 1981-85

(In millions of Dominican pesos)

	1981	1982	1983	Preliminary 1984	Preliminary 1984 1/	Proj. 1985 1/
			I. Central Bank			
Net international reserves	-322.3	-678.6	-428.1	-335.9	-940.5	-636.1
Assets	283.5	172.4	204.3	268.0	750.4	826.0
Liabilities	-605.8	-851.0	-632.4	-603.9	-1,690.9	-1,462.1
Domestic credit	1,294.0	1,736.7	2,108.6	2,311.5	2,311.5	2,424.2
Net claims on the public sector	688.0	970.5	1,253.8	1,333.3	1,333.3	1,333.3
Central government	(536.1)	(732.0)	(916.1)	(935.4)	(935.4)	(935.4)
Public financial institutions	(146.5)	(151.2)	(149.6)	(148.0)	(148.0))	(148.0)
Rest of public sector	(5.4)	(87.3)	(188.1)	(249.9)	(249.9))	(249.9)
Credit to commercial banks	444.5	530.2	599.0	568.4	568.4	568.4
Credit to rest of the financial system	133.0	157.9	190.7	215.9	215.9	215.9
Net unclassified assets	28.5	78.1	65.1	193.9	193.9	306.6
Revaluation account	--	--	--	--	2,185.7 2/	2,185.7 2/
Medium- and long-term foreign liabilities	259.0	359.1	829.4	878.4	2,459.5	2,547.7
Other liabilities	-167.5	-61.3	67.1	81.9	81.9	181.9
Monetary base	880.2	760.3	784.0	1,015.3	1,015.3	1,244.2
Currency in circulation	323.8	357.1	414.7	592.8	592.8	724.2
Cash in vaults	72.1	74.1	72.2	98.9	98.9	107.1
Reserve deposits	484.3	329.1	297.1	323.6	323.6	412.9
Memorandum item						
Net domestic assets	718.2	1,109.8	915.0	1,027.6	1,632.2	1,467.4
			II. Reserve Bank			
Net international reserves	-12.5	-0.2	-38.6	-22.7	-63.6	-63.6
Assets	51.6	52.4	17.1	17.8	49.8	...
Liabilities	-64.1	-52.6	-55.7	-40.5	-113.4	...
Monetary reserves and currency holdings	21.1	13.2	5.4	98.0	98.0	120.8
Domestic credit	685.8	747.3	739.6	850.7	891.6	969.2
Net claims on the public sector	302.4	410.4	414.7	469.0	469.0	469.0
Central government	(83.0)	(86.4)	(50.7)	(92.8)	(92.8)	(...)
Public financial institutions	(44.0)	(46.8)	(49.2)	(51.1)	(51.1)	(...)
Rest of public sector	(175.4)	(277.2)	(314.8)	(325.1)	(325.1)	(...)
Credit to rest of the financial system	8.1	9.9	15.0	11.3	11.3	--
Credit to private sector	380.6	365.9	387.5	428.0	428.0	516.9
Net unclassified assets 3/	-5.3	-38.9	-77.6	-57.6	-16.7	-16.7
Liabilities to monetary authorities	364.4	446.4	421.3	472.9	472.9	472.9
Liabilities to rest of the financial system 4/	23.8	33.6	35.2	49.5	49.5	60.4
Liabilities to private sector	306.2	280.3	249.9	403.6	403.6	493.1
Demand deposits	61.3	50.6	14.2	78.0	78.0	...
Time and savings deposits	116.6	131.7	132.5	168.1	168.1	...
Other liabilities (net)	128.3	98.0	103.2	157.5	157.5	...

Table 14. Dominican Republic: Summary Accounts of the Banking System, 1981-85 (Concluded)

(In millions of Dominican pesos)

	1981	1982	1983	Preliminary 1984	Preliminary 1984 1/	Proj. 1985 1/
III. Private Commercial Banks						
Net international reserves	-56.3	-21.9	-4.3	-3.9	-10.9	-10.9
Assets	220.9	239.5	25.6	40.7	114.0	...
Liabilities	-277.2	-261.4	-29.9 5/	-44.6	-124.9	...
Monetary reserves and currency holdings	366.8	317.2	381.6	430.6	430.6	507.9
Domestic credit	757.5	883.5	1,012.4	1,118.5	1,125.5	1,368.4
Net claims on public sector	5.2	-1.8	26.1	19.6	19.6	19.6
Central government	(10.7)	(8.9)	(11.0)	(15.1)	(15.1)	(...)
Public financial institutions	(-6.5)	(-11.5)	(3.8)	(-0.8)	(-0.8)	(...)
Rest of public sector	(1.0)	(0.8)	(11.3)	(5.3)	(5.3)	(...)
Credit to rest of the financial system 4/	34.4	30.0	37.6	48.1	48.1	48.1
Credit to private sector	639.3	747.8	871.1	985.0	985.0	1,227.9
Net unclassified assets	78.6	107.5	77.6	65.8	72.8	72.8
Liabilities to monetary authorities	83.1	85.6	97.1	96.5	96.5	96.5
Liabilities to rest of the financial system	28.3	48.3	79.8	106.7	106.7	130.3
Liabilities to private sector	956.6	1,044.9	1,212.8	1,342.0	1,342.0	1,638.6
Demand deposits	240.1	289.3	318.1	425.8	425.8	...
Time and savings deposits 6/	436.5	531.1	586.7	611.7	611.7	...
Other liabilities (net)	280.0	224.5	308.0	304.5	304.5	...
IV. Consolidated Accounts of the Banking System						
Net international reserves of the banking system	-391.1	-700.7	-471.0	-362.5	-1,015.0	-710.6
Assets	556.0	464.3	247.0	326.5	914.2	...
Liabilities	-947.1	-1,165.0	-718.0	-689.0	-1,929.2	...
Domestic credit	2,288.8	2,823.9	3,292.8	3,735.5	3,783.4	4,119.2
Net claims on the public sector	995.6	1,379.1	1,694.6	1,821.9	1,821.9	1,821.9
Central government	(629.8)	(827.3)	(977.8)	(1,043.2)	(1,043.2)	(...)
Public financial institutions	(184.0)	(186.5)	(202.6)	(198.2)	(198.2)	(...)
Rest of public sector	(181.8)	(365.3)	(514.2)	(580.5)	(580.5)	(...)
Credit to rest of the financial system 4/	175.5	197.8	243.3	275.3	275.3	264.0
Credit to the private sector	1,019.9	1,113.7	1,258.6	1,413.0	1,413.0	1,744.8
Net unclassified assets 7/	97.8	133.3	96.3	225.3	273.2	288.5
Revaluation account	--	--	--	--	2,185.7 2/	2,185.7 2/
Medium- and long-term foreign liabilities	259.0	359.1	829.4	878.4	2,459.5	2,547.7
Liabilities to the rest of the financial system	52.1	81.9	115.0	156.2	156.2	190.7
Liabilities to the private sector	1,586.6	1,682.2	1,877.4	2,338.4	2,338.4	2,855.9
Currency in circulation	323.8	357.1	414.7	592.8	592.8	724.2
Demand deposits	301.4	339.9	332.3	503.8	503.8)	
Time and savings deposits	553.1	662.8	719.2	779.8	779.8)	1,611.7
Other liabilities (net)	408.3	322.4	411.2	462.0	462.0	520.0

Sources: Central Bank of the Dominican Republic; and Fund staff estimates and projections.

1/ Foreign currency transactions valued at RD$2.8 per U.S. dollar.
2/ Foreign exchange valuation adjustment.
3/ Includes official capital.
4/ Includes savings and loan associations and nonbank financial institutions.
5/ Balance sheet data adjusted downward by RD$8.2 million of liabilities included in refinancing with commercial banks.
6/ Includes private capital and other deposits.
7/ Includes interbank float.

Table 15. Dominican Republic: Terms of Trade and Their Effect on the Trade Balance

	1981	1982	1983	Prel. 1984	Proj. 1985
	(1981 = 100)				
Terms of trade	100.0	86.6	87.1	90.6	83.0
Export prices	100.0	87.8	90.1	94.5	87.2
Import prices	100.0	101.4	103.4	104.3	105.0
	(Annual percentage change)				
Terms of trade	4.1	-13.4	0.6	4.0	-8.4
Export prices	11.4	-12.2	2.6	4.9	-7.7
Import prices	7.0	1.4	2.0	0.9	0.7
	(In millions of U.S. dollars)				
Change in trade balance	294.1	-226.0	-7.3	105.9	41.1
Due to:					
Terms of trade effect	3.3	-165.2	-5.1	27.0	-75.3
Change in export prices	(109.7)	(-144.9)	(20.0)	(38.5)	(-66.5)
Change in import prices	(-106.4)	(-20.3)	(-25.1)	(-11.5)	(-8.8)
Volume effect	290.8	-60.8	-2.2	78.9	116.4
Change in export volume	(116.4)	(-275.5)	(-2.4)	(40.2)	(2.6)
Change in import volume	(174.4)	(214.7)	(0.2)	(38.7)	(113.8)

Sources: Statistical Appendix Tables 16 and 17; and Fund staff estimates and projections.

Table 16. Dominican Republic: Exports by Principal Commodity Groups

(Value in millions of U.S. dollars; volume in thousands of metric tons or troy ounces; and unit value in U.S. dollars per metric ton unless otherwise stated)

	1981	1982	1983	Prel. 1984	Proj. 1985
Total exports, f.o.b.	1,188.0	767.6	785.2	863.9	800.0
Major agricultural exports	753.6	487.2	460.3	526.8	442.3
Raw sugar					
Value	513.2	265.5	263.6	276.1	205.0
Volume	847.5	833.3	917.7	834.6	827.7
Unit value	605.5	318.6	287.2	330.8	247.7
Unit value (per 100 lbs)	27.5	14.5	13.0	15.0	11.2
Refined sugar and byproducts					
Value	47.2	43.1	35.4	44.2	30.2
Unprocessed coffee					
Value	62.2	90.6	76.3	94.3	86.4
Volume	26.8	34.0	29.7	34.3	30.9
Unit value	2,320.9	2,664.1	2,567.8	2,749.0	2,796.1
Unit value (per 100 lbs.)	105.2	120.8	116.5	124.7	126.8
Processed coffee					
Value	13.6	5.0	0.1	--	0.1
Raw cocoa					
Value	44.8	52.9	55.5	68.9	64.8
Volume	27.2	38.7	34.4	31.8	34.0
Unit value	1,647.1	1,366.2	1,612.0	2,166.7	1,905.8
Unit value (per 100 lbs.)	74.6	62.0	73.1	98.3	86.5
Processed cocoa					
Value	5.3	6.1	5.4	7.3	11.5
Tobacco leaf					
Value	65.6	21.4	21.8	28.5	33.1
Volume	39.2	12.1	13.5	18.7	20.0
Unit value	1,673.5	1,777.5	1,617.0	1,524.1	1,653.8
Unit value (per 100 lbs.)	76.0	80.6	73.3	69.1	75.0
Tobacco products					
Value	1.7	2.6	2.2	7.5	11.2
Major mineral products	334.1	193.0	248.0	233.7	227.7
Bauxite					
Value	15.7	5.2	--	--	--
Volume	457.2	140.5	--	--	--
Unit value	34.3	37.3	--	--	--
Ferronickel					
Value	110.5	24.2	83.5	101.9	115.0
Volume	49.1	14.1	53.8	58.6	60.0
Unit value	2,250.5	1,709.6	1,550.8	1,738.9	1,916.7
Gold alloy					
Value	186.4	146.6	149.5	122.1	105.0
Volume (troy ounces)	407.8	386.3	354.0	338.3	321.0
Silver alloy					
Value	21.5	17.0	15.0	9.7	7.7
Volume (troy ounces)	2,033.6	2,197.0	1,328.1	1,204.5	1,060.0
Other exports	100.3	87.4	76.9	103.4	130.0

Sources: Central Bank of the Dominican Republic; and Fund staff estimates and projections.

Table 17. Dominican Republic: Imports by Major Category 1/

	1981	1982	1983	Prel. 1984	Proj. 1985
(In millions of U.S. dollars)					
Total imports	1,451	1,257	1,282	1,252	1,147
Petroleum and derivatives	497	451	461	507	450
Coal	--	--	--	--	15
INESPRE	101	54	64	81)	
Other	853	752	757	664)	682
(Percentage change)					
Total imports	-3.2	-13.4	2.0	-2.3	-8.4
Petroleum and derivatives	10.8	-9.2	2.2	10.0	-11.2
Other	-8.3	-5.6	1.9	-9.3	-6.4

Sources: Central Bank of the Dominican Republic; and Fund staff estimates and projections.

1/ Based on customs data.

Table 18. Dominican Republic: Monthly Average Premia in the Free Exchange Market Over the Official Buying and Selling Rates for the U.S. Dollar 1/

	1980		1981		1982		1983		1984	
	Buying	Selling	Buying	Selling	Buying	Selling	Buying	Selling	Buying	Selling
January	25.10	26.62	25.09	26.27	33.43	34.53	50.47	52.30	91.3	93.7
February	24.01	25.40	26.56	27.77	37.68	39.00	49.11	50.91	192.0	196.5
March	24.36	25.65	26.91	28.09	43.50	44.76	49.39	50.53	177.0	180.7
April	26.60	27.82	27.16	28.20	46.16	47.58	50.95	52.66	176.2	179.4
May	27.69	29.15	26.59	27.77	43.15	44.67	55.24	56.60	174.3	177.3
June	27.84	29.48	26.67	27.75	46.25	47.81	55.11	56.41	175.6	177.2
July	24.75	26.00	26.28	27.48	47.92	49.02	57.22	58.38	179.6	181.2
August	25.02	26.09	26.05	27.24	44.92	46.16	58.45	59.58	180.8	182.1
September	24.57	25.85	27.31	28.58	47.61	48.88	58.53	59.68	178.6	179.9
October	23.61	24.91	28.34	29.47	50.59	51.70	73.19	75.14	185.4	186.9
November	22.58	23.92	29.86	30.99	50.16	51.85	83.97	87.09	196.6	198.0
December	22.06	23.31	29.13	30.58	49.29	50.44	79.00	81.00	207.0	210.1
Annual average	24.85	26.18	27.16	26.35	45.05	46.36	60.05	61.69	176.2	178.6

Source: Central Bank of the Dominican Republic.

1/ The official rate was RD$1 per U.S. dollar through 1984.

Table 19. Dominican Republic: Real and Nominal Effective Trade Weighted Exchange Rates, 1981-84 1/

(1980 = 100)

	Real Effective Exchange Rate	Nominal Effective Exchange Rate
1981		
Q_1	100.6	102.2
Q_2	102.4	105.0
Q_3	102.8	107.0
Q_4	100.5	105.0
1982		
Q_1	101.8	104.6
Q_2	101.7	104.3
Q_3	100.2	103.9
Q_4	98.6	101.7
1983		
Q_1	96.0	98.8
Q_2	95.1	98.8
Q_3	95.2	98.5
Q_4	88.3	90.9
1984		
Q_1	76.7	74.7
Q_2	61.2	55.7
Q_3	65.0	54.2
Q_4	68.5	52.8

Source: Fund staff calculations.

1/ The calculations exclude oil imports. Moreover, they are based on a composite exchange rate which attempts to capture the shifts in transactions from the official to the parallel market.

Table 20. Dominican Republic: External Arrears at End-1984

(In millions of U.S. dollars)

Paris Club creditors	169.0
Commercial banks	104.2
Letters of credit	33.5
Credit Agricole	63.8
Arrears included in Central Bank liabilities	112.5
Other (including international organizations)	18.4
Total	501.4

Source: Fund staff estimates.

Stand-By Arrangement - Dominican Republic

Attached hereto is a letter, dated February 28, 1985, with an annexed technical memorandum from the authorities of the Dominican Republic requesting a stand-by arrangement and setting forth the objectives and policies that the Government of the Dominican Republic intends to pursue. To support these objectives and policies, the International Monetary Fund grants this stand-by arrangement in accordance with the following provisions:

1. For the period from April , 1985 to April , 1986, the Dominican Republic will have the right to make purchases from the Fund in an amount equivalent to SDR 78.5 million, subject to paragraphs 2, 3, 4, 5, and 6 below, without further review by the Fund.

2. (a) Purchases under this stand-by arrangement shall not, without the consent of the Fund, exceed the equivalent of SDR 28,025,000 until August 15, 1985, the equivalent of SDR 44,725,000 until October 31, 1985, and the equivalent of SDR 61,425,000 until February 28, 1986.

(b) None of the limits in (a) above shall apply to a purchase under this stand-by arrangement that would not increase the Fund's holdings of the Dominican Republic's currency in the credit tranches beyond 25 percent of quota.

3. Purchases under this stand-by arrangement shall be made from ordinary resources.

4. The Dominican Republic will not make purchases under this stand-by arrangement that would increase the Fund's holdings of the Dominican Republic's currency in the credit tranches beyond 25 percent of quota

(a) during any period in which the data at the end of the last reporting period show that:

(i) the limit on the combined central bank and reserve bank net credit to the public sector set forth in Table 1 annexed to the attached letter is not observed;

(ii) the cumulative reduction of the net domestic assets of the Central Bank of the Dominican Republic set forth in Table 2 annexed to the attached letter; is not observed;

(iii) the target for the net foreign assets of the Central Bank set forth in Table 3 annexed to the attached letter is not observed;

(iv) the cumulative reduction through cash payments in external arrears set forth in Table 4 annexed to the attached letter is not observed; or

(v) the ceilings on disbursements under nonconcessional external public and publicly guaranteed debt, set forth in Table 5 annexed to the attached letter, are not observed;

(b) during any period after August 14, 1985 if understandings are not reached between the Fund and the Dominican Republic on exchange rate policy, interest rate policy, the reduction of external payments arrears, external financing, and on the establishment of quantitative performance criteria for the remaining period of the arrangement, or while such understandings are not being observed; or

(c) during any period after February 27, 1986 if understandings are not reached between the Fund and the Dominican Republic for the remaining period of the arrangement on exchange rate policy, interest rate policy, the reduction of external payment arrears and external financing, or while such understandings are not being observed; or

(d) during the entire period of the stand-by arrangement, if the Dominican Republic:

(i) imposes or intensifies restrictions on payments and transfers on current international transactions; or

(ii) introduces or modifies multiple currency practices other than the reduction or elimination of existing multiple currency practices; or

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

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

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

5. The Dominican Republic will not make purchases under the stand-by arrangement during any period of the arrangement in which the member has an overdue financial obligation to the Fund or is failing to meet a repurchase expectation pursuant to the guidelines on Corrective Action in respect of a noncomplying purchase.

6. The Dominican Republic's right to engage in the transactions covered by this stand-by 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 the Dominican Republic. When notice of a decision of formal ineligibility or of a decision to consider a proposal is given pursuant to this paragraph 6, purchases under this arrangement will be resumed only after consultation has taken place between the Fund and the Dominican Republic and understandings have been reached regarding the circumstances in which such purchases can be resumed.

7. Purchases under this stand-by 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 the Dominican Republic, the Fund agrees to provide them at the time of the purchase.

8. The Dominican Republic shall pay a charge for this stand-by arrangement in accordance with the decisions of the Fund.

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

(b) Any reductions in the Dominican Republic'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.

10. During the period of the stand-by arrangement the Dominican Republic shall remain in close consultation with the Fund. These consultations may include correspondence and visits of officials of the Fund to the Dominican Republic or of representatives of the Dominican Republic to the Fund. The Dominican Republic 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 the Dominican Republic in achieving the objectives and policies set forth in the attached letter.

11. In accordance with paragraph 30 of the attached letter, the Dominican Republic will consult with 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 in 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 the Dominican Republic has outstanding purchases in the upper credit tranches, 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 the Dominican Republic's balance of payments policies.

Santo Domingo,
February 28, 1985

Dear Mr. de Larosiere:

1. The purpose of this letter is to inform you of the results of the economic policy measures adopted in the Dominican Republic in 1984 and to report to you the Government's economic objectives and targets for 1985. On the basis of the financial program for 1985 outlined below, we hereby request the use of Fund resources under a one-year stand-by arrangement amounting to SDR 78.5 million or 70 percent of the Dominican Republic's quota.

2. Since the present Administration assumed office in August 1982, its objective has been to reorganize and strengthen the national economy, which had been adversely affected by the world economic crisis. Perhaps the greatest obstacles to the total achievement of these economic objectives were the deviations and distortions in the economy created by the adoption of a policy of transferring resources from the productive sector to the consumption sector through a complex system of subsidies. This policy was manageable at a time when the terms of trade were favorable to the Dominican Republic, when international energy prices were relatively low, and when the Central Bank had sufficient foreign exchange to support such a policy. As these reserves were exhausted due to inappropriate policies, such as the creation of inflationary resources and a high level of external debt, the situation changed adversely for the country and the distortions became more apparent. The Dominican Republic started experiencing serious balance of payments deficits which, coupled with a marked deterioration in the public finances, left the Central Bank without foreign exchange reserves and led to a very large accumulation of external payments arrears. Economic activity slowed and the value of the Dominican peso declined in the parallel market. The growing discrepancy between the official exchange rate and the rate in the parallel market has intensified the distortions in the allocation of resources.

3. In these circumstances, the new administration adopted a program of economic recovery that was supported by the International Monetary Fund with an extended arrangement which started on January 21, 1983. This program sought to correct the serious disequilibria that had occurred in the economy. It emphasized, first, the strengthening of the public finances and domestic savings in order to correct the internal disequilibrium and, secondly, the reform of the exchange system in order to correct the distortions that had been created and were compounding the external disequilibrium. The elimination of both the internal and the external disequilibria was considered crucial for any improvement in the productive capacity of the country.

4. Efforts to achieve these objectives centered on reducing the public sector deficit to lessen the dependence on central bank credit as a source of government financing. It was felt that such an adjustment of the public finances would reduce the pressure on the foreign reserves of the Central Bank, on the exchange rate of the peso in the parallel market and, consequently, on the price level. The central government deficit was to be reduced through an improvement in tax collections resulting from a package of tax measures that was presented to the Congress at the end of 1982 and most of which was approved early in 1983. This package included among other things the introduction of a sales tax of the value-added type (ITBI). The rest of the improvements were to come from holding down central government expenditures and streamlining the operations of public enterprises.

5. With respect to monetary and credit policies, the expansion of central bank credit was strictly controlled by the adoption of ceilings on credit to the public sector so as to reduce the pressure that expansion of such credit was exerting on the balance of payments and on domestic prices. To encourage an expansion of the financial savings of the private sector, a high-yield financial certificate was introduced and, at the same time, the interest rates on other financial instruments were also raised.

6. With respect to exchange rate policy, the program attempted to encourage traditional exports by giving them partial access to the exchange rate of the parallel market. It was felt that in this way not only would the availability of foreign exchange be increased but also production and employment opportunities would rise. To eliminate the imbalance in the official foreign exchange market, the program contemplated an accelerated transfer of certain payments from the official to the parallel market. The program also envisaged a reduction of external payments arrears of over US$100 million and their total elimination by the end of the third year of the program. The use of short- and medium-term external financing was also restricted.

7. In reviewing the performance under the program in 1983, it should be noted that while some targets were met, the degree of adjustment sought was not achieved. The deficit of the nonfinancial public sector was larger than programmed and, although lower than that of 1982, it required almost the same level of domestic financing. The balance of payments improved little in 1983: the current account deficit declined only slightly; and the Dominican peso depreciated in the parallel market. Nonetheless, some important objectives were met: the Dominican Republic experienced one of the lowest inflation rates of the hemisphere; real GDP grew by nearly 4 percent; and a part of the external debt with commercial banks was rescheduled.

8. The difficulties in achieving major adjustment during the first year of the program and the subsequent delays in coming to an agreement on the 1984 program created uncertainty about the timely implementation of further measures required to meet the economic crisis. This led to

speculative pressures on the exchange rate in the parallel market and on the reserves of the Central Bank. The Government at that time recognized that the depreciation of the Dominican peso that had already taken place in the parallel market was reflected in most balance of payments transactions. The Government, therefore, decided to unify the exchange rate as soon as possible.

9. To this end, and in order to close the gap in the official exchange market, in April 1984 the Government transferred to the parallel market all payments for the import of goods and services, excluding petroleum. In conjunction with these measures, almost all nontraditional exports were effectively transferred to the parallel market and traditional exports were granted a preferential exchange rate of RD$1.48 per U.S. dollar.

10. To allow this exchange rate adjustment to produce the desired effects, it was accompanied by increases in the domestic prices of all products affected by the exchange rate adjustment including those of goods and services produced by public enterprises. This provoked serious social disturbances and the necessary increase in oil prices had to be postponed in view of the need to restore public order and peace.

11. By this time, six months had passed and understandings with the Fund within the framework of the extended arrangement were no longer feasible. Instead, the Government proceeded to implement an interim economic program that was communicated to you on August 21, 1984--the transitional program. This transitional program was designed to allow time for the formulation of policies for 1985 which could be supported by resources from the Fund. The main objectives of this program were: (a) to establish a basis for eventual unification of the exchange rate; (b) an improvement in the net foreign asset position of the Central Bank; and (c) a reduction of the nonfinancial public sector deficit to a level compatible with no use of Central Bank or Reserve Bank credit in the second half of 1984.

12. As a step toward unifying the exchange markets, the authorities decided to raise the price of petroleum products by over 60 percent. This made it possible to adjust the exchange rate applied to oil imports to RD$1.5 per U.S. dollar, excluding fuel imported by the Electricity Corporation (CDE). The Central Bank's losses arising from the differences between the selling and buying rates of foreign exchange for some transactions in the official market would be offset by profits from the sale in the parallel market of the surplus of foreign exchange expected to be obtained in the official market. Developments in the last few months of 1984 indicated that the exchange position of the Central Bank had deteriorated, due partly to lower-than-expected foreign exchange receipts from exports and partly because the transitional program had not produced the increased foreign financial assistance which had been expected. External payments arrears increased by about US$250 million during the year to reach approximately US$500 million at the end of 1984.

13. In the fiscal area, the increased prices of petroleum products produced larger tax revenues for the Government, and the exchange rate applied for the collection of customs duties was raised from RD$1.7, the rate which had been applied since January 1, 1984, to RD$2 per U.S. dollar. Measures were also taken to improve tax administration and to increase the rates of some consumption taxes as well as the international departure tax. On the expenditure side, considerable cuts were made in public investment due to the inability to provide the required domestic counterpart funds for those projects financed with foreign resources. Given the strict controls which the Government applied, expenditure in the last part of the year was financed without recourse to domestic credit. Progress also was made in improving the efficiency of some public enterprises. The Corporation of State Enterprises (CORDE) achieved a surplus in its 1984 operations. The State Sugar Company (CEA) reduced its financing needs in 1984 due to the depreciation of the peso and to an adjustment in domestic prices. The Electricity Corporation (CDE) improved its monitoring system in order to reduce losses from illegal use of electricity. The deficit of the Price Stabilization Institute (INESPRE) was reduced because of some increase in the sale price of imported foodstuffs.

14. As a consequence of the corrective price adjustments that have taken place, it is estimated that the average inflation rate was around 21 percent for the 12-month period ended November 1984. In order to partially offset the fall in real wages, in May 1984 the Congress approved the Government's proposal to increase the minimum monthly wage, which had been RD$125 for the past four years, to RD$175; wages in the RD$175 to RD$300 band were increased by 10 percent. The additional resources required by the Central Government to finance this wage increase were obtained in large part from new consumption taxes.

15. As explained above, for 1985 the Government intends to put into effect policies directed toward reinforcing the medium-term adjustment program and further correcting the distortions that have characterized the economy in recent years. In the area of exchange rate policy, the Government unified the exchange markets as of January 23, 1985. Since then all exchange transactions are being carried out at an exchange rate determined freely by the market. The public sector entities will revalue their assets and liabilities denominated in foreign currency at the exchange rate prevailing on that date and will record their future operations at the corresponding exchange rate. The compulsory surrender of foreign exchange proceeds from exports will continue. Since the unification of the exchange market, traditional exports and certain services are receiving the market exchange rate minus a temporary exchange tax of 36 percent, and exports of nontraditional goods are receiving the market rate less a temporary exchange tax of 5 percent. These taxes will be used to partly offset the additional cost to the public sector caused by the unification of the rate and the rejection by the Senate of the Republic of the tax package proposed in the budget for 1985. In spite of the exchange tax, the domestic currency receipts of the traditional export sector will increase as the exchange rate applicable to them will improve significantly. The rate of the tax applied to the

nontraditional sector is considered to be sufficiently small so as not to have any significant adverse impact. In the context of the review of the program envisaged in paragraph 30 of this letter, the Dominican Republic will reach understandings with the Fund for the progressive reduction of these taxes and on permanent measures that will enable the Government to eventually replace them both. We believe that these measures will restore public confidence, revitalize the export sector, and eliminate the Central Bank's losses from foreign exchange operations and arrest the decline in its foreign exchange reserves that has been taking place for many years.

16. With regard to the domestic objectives, one fundamental component of the Government's adjustment program is the strengthening of the public finances. The Government intends to reduce the net financing requirements of the public sector from 7.5 percent of GDP in 1984 to 4.9 percent in 1985. This objective is consistent with available foreign financing in 1985. The 1985 budgets of the Central Government and the other public sector entities are being executed on the basis of an exchange rate of RD$2.8 per U.S. dollar, strict control of current expenditure, and the estimated effect of the new tax and price measures needed to assure the elimination of any requirement for financing from the Central Bank and the Reserve Bank.

17. The budget of the Central Government for 1985 was presented to the Congress on November 28, 1984. The estimates incorporated in the budget included a series of tax measures expected to generate RD$131 million in 1985, involving the following items: (a) the elimination of exemptions from the ITBI, with an expected yield of RD$47 million; (b) the application of ITBI taxes to alcoholic beverages and processed tobacco, with an expected yield of RD$20 million; (c) a reduction of 50 percent in the exemptions from taxes on imports under Law No. 299, with an expected yield of RD$29 million; (d) the application of a minimum rate of 20 percent ad valorem to enterprises benefiting from special tax status under Congressional Law (Law No. 666), with an expected yield of RD$20 million; and (e) the extension of ITBI to certain services, with an expected yield of RD$15 million. The tax package included, in addition, the imposition, through administrative order, of a levy of US$10 per person on tourist arrivals, which is expected to generate RD$12 million in 1985.

On January 9, 1985 the Senate of the Republic rejected the above tax legislation proposals and on January 12, 1985 modified the proposed budget. As a result of the rejection of the proposed tax legislation, and in order to conform to the requirement that the program be fully financed, it has been necessary to increase to a greater extent than that originally programmed the levels of electricity tariffs (50 percent) and the prices of petroleum products (64 percent) with corresponding consequences on domestic prices. Moreover, it has been necessary to reduce the level of current central government expenditure by RD$23 million. Until Congress takes a final decision on the tax legislation and the budget of the Central Government for 1985--in accordance with the provisions of the Constitution--the 1984 budget will continue to be implemented. In the execution of the budget the following measures have been incorporated: (a) the adjustment of the exchange rate undertaken on January 23, 1985 on the basis of an exchange rate of RD$2.8 per U.S. dollar; (b) the payment of interest to the Central Bank in the amount of RD$105 million in respect of securities of the Central Government acquired by that institution in previous years; (c) the application of the exchange rate of the free market in the calculation of import duties instead of the exchange rate of RD$2 per U.S. dollar which used to be applied before--this measure is expected to yield RD$100 million on an annual basis; and (d) the increases in prices of petroleum products, which should yield RD$184 million on an annual basis.

18. With regard to the public enterprises, the general policy principle will be to ensure that they fully cover their current costs and gradually make progress toward generating an adequate return on their investment. In 1984 the prices of public enterprises, including the CORDE group, were adjusted to cover the higher operating costs resulting from the transfer of their imports to the parallel market and the higher cost of energy. This policy will continue in 1985.

19. The CEA, as well as the private sugar mills, will receive additional revenue in 1985 because of the exchange rate adjustment. In order to provide CEA with a further RD$20 million in revenue, domestic prices of sugar and molasses were recently increased. Furthermore, the CEA is implementing a program, partially financed by the World Bank, to modernize the sugar mills and the transportation system and to improve its administration. It is also implementing joint projects with the private sector, such as the cultivation of the African palm and pineapple in order to diversify its production activities.

20. The financial situation of the CDE remains precarious due to problems that built up between 1972 and 1982 in such areas as losses in the generation and distribution systems; high cost of fuel per unit generated, due to the lack of preventive maintenance; defective planning and execution of the investment program; and a tariff structure that heavily subsidizes the large residential and commercial and industrial consumers, which tends to encourage waste. The loss of purchasing power of the Dominican peso has raised the operating costs of the CDE in Dominican pesos by a factor of 2.5 over the past two years. However, tariffs had not been increased accordingly since June 1982 and the higher costs were being subsidized through the exchange system. This subsidy rose to approximately RD$300 million in 1984. CDE's administration has been implementing programs to improve the operational efficiency of the enterprise and these are already showing positive results. The main areas in which additional efficiency can be expected are: (a) reducing generation and distribution losses from 30 percent in 1984 to 21 percent in 1987; and (b) reducing electricity generation costs from US$0.08 per kwh in 1984 to US$0.037 per kwh in 1987 mainly by substituting coal for oil in thermal electricity generation and by the entry into operation of hydropower. In spite of these improvements, the CDE will continue to experience large cash deficits if the tariff structure is not corrected. To this end, a new system of tariffs has been adopted to fully

eliminate the deficits. The new tariff includes an initial adjustment for large residential and commercial consumers that will result in an increase of 33 percent in the average tariff, and a monthly adjustment of 2 percent for those who use more than 300 kwh per month which is to be applied until the deficit is eliminated. The expected increase in revenue will be around RD$125 million in 1985. The remaining deficit, estimated at RD$225 million, will be compensated by transfers of proceeds from the exchange taxes.

21. The Government will intensify its effort to improve the operations of the Price Stabilization Institute (INESPRE). INESPRE's budget has therefore been formulated in such a way as to reduce its deficit to RD$67 million. To this end, the prices of various products sold by INESPRE have been raised significantly. INESPRE has also abandoned its participation in the marketing of certain loss-making products.

22. The corrective price adjustments that have taken place in 1985 will not permit an immediate reduction of the inflation rate. However, given that the creation of demand pressures will be avoided, it is hoped that the monthly inflation rate can be brought down by the end of 1985 to levels prevailing in previous years, although the average increase in prices in 1985 will still be of a magnitude similar to that of 1984. To avoid an inflationary spiral, the Government intends to implement a policy of wage restraint. The budgets of the Central Government and the decentralized institutions do not include provisions for wage increases. Such increases will be authorized only to the extent that other expenditure can be reduced or through the identification of new fiscal resources, without recourse to financing. However, to protect the purchasing power of low-income groups, the Government proposes to maintain certain subsidies on basic foodstuffs and public transport. On the other hand, the Government has submitted to Congress two draft tax laws to obtain resources with which to cover the Christmas bonus and produce an increase in civil servants' salaries of similar magnitude to the 10 percent wage adjustment granted in May 1984.

23. The efforts being made to strengthen the public finances, and the reform of the exchange system, will help to improve the Central Bank's financial situation. Given the target for the increase in net international reserves, mentioned at the end of paragraph 26, and the need to avoid aggravating inflationary pressures through an excessive increase in the money supply, the Central Bank will need to pursue a very cautious credit policy. Therefore, the Central Bank will not extend credit to the public sector, including the Reserve Bank, other than for strictly seasonal needs. Although, the Central Government has included in its budget a payment of RD$105 million in interest to the Central Bank, the Bank's operating losses--stemming mainly from the payment of interest on the debt it took over as the result of the 1983 debt restructuring--will still be considerable. It is anticipated that these losses will be covered through the exchange taxes. The Bank also expects to attract resources from commercial banks and financial institutions in accordance with the monetary and interest rate policies described in

the following paragraphs. These resources will permit the Central Bank to reduce considerably its net domestic assets in 1985, without requiring a contraction in its portfolio.

24. For the purpose of having better control over the liquidity of the financial system, the Central Bank will issue notes and bonds, including those from its own holdings. In the event that the targeted amounts of such securities cannot be placed in the market, the legal reserve requirements for commercial banks will be raised.

25. In order to increase the flow of private financial savings into the formal financial system and to improve the allocation of resources, the Government has increased interest rates. The rules applicable to the financial certificates which were authorized for the first time in late 1982 were recently revised to allow a term of six months and a minimum denomination of RD$10,000. The minimum interest rate was set at 9 1/2 percent and the maximum at 18 percent. The financial intermediaries may negotiate their rates within this range, which will be subject to periodic review in the light of interest rate developments in international markets, the domestic rate of inflation, and the market exchange rate of the peso. Interest rates, such as other deposit interest rates, bank lending rates, the rediscount rates charged by the Central Bank, and the rates which it pays on reserve deposits, were adjusted upward in January 1985. The legal reserve requirements applicable to the Reserve Bank were recently amended to eliminate the exemption formerly in effect for public sector deposits received by the Bank. The Reserve Bank is subject to the same legal reserve regulations as those applicable to the other commercial banks on any increase in deposits. The Bank's legal reserve shortfalls could not be eliminated immediately without causing serious problems, but a timetable has been established for the gradual reduction of such shortfalls. It also has been established that the ratio of the Bank's cash reserves to deposits subject to reserve requirements may not fall below the level of December 31, 1984. Furthermore, the Reserve Bank will be obligated to pay extraordinary charges if it were to make use of central bank funds through overdrafts in the clearing facilities.

26. It is expected that the deficit (before rescheduling) in the current account of the balance of payments will show an improvement in 1985, to 0.6 percent of GDP, compared with an estimated 4.3 percent in 1984, mainly on account of the expected reduction in oil imports and the continued expansion of receipts from tourism and nontraditional exports. However, the overall balance of payments outturn in 1985 will be dominated by the heavy burden of servicing the debt. Therefore, the Government will not approve barter operations involving traditional exports whose foreign exchange proceeds are scheduled to accrue to the Central Bank. As an integral part of the program, the Government of the Dominican Republic will have to obtain a far-reaching restructuring of its external liabilities, including arrears. As regards the net international reserves of the Central Bank the objective is to achieve an increase of US$109 million in 1985.

27. The Government is determined to resolve the critical problem of the Dominican Republic's debt service burden. To this end, management of the external debt must be oriented toward meeting external financing needs through long-term borrowing. However, use of external loans with a maturity of less than 12 years will continue in 1985, because certain projects are being financed with such loans. During 1985 there will be net repayments of US$19.3 million in respect of external public debt with maturities of less than one year, and disbursements of external public debt with maturities of 1 to 12 years will be limited to US$198.5 million.

28. The Government of the Dominican Republic undertakes not to introduce any new multiple currency practices, or impose or intensify restrictions on payments and transfers for current international transactions, or enter into bilateral payments agreements that are inconsistent with Article VIII of the Articles of Agreement of the International Monetary Fund, or impose or intensify import restrictions for balance of payments reasons.

29. The performance criteria which will be used in monitoring progress in the implementation of the program are presented in the Technical Memorandum attached to this letter.

30. During the period of the stand-by arrangement the authorities will consult with the International Monetary Fund, in accordance with the Fund's policies on such consultations, regarding progress made in implementing the program described in this letter of intent and any other policy measure they may deem appropriate for the achievement of these objectives. At any rate, no later than August 15, 1985, the Government will consult with the Fund in order to establish appropriate performance criteria for end-September and end-December 1985. Furthermore, the Government will review quarterly with the staff the progress made in the implementation of the program.

Sincerely yours,

/s/
Hugo Guiliani Cury
Governor, Central Bank

/s/
Orlando Haza
Technical Secretary of the Presidency

/s/
Manuel Cocco
Secretary of Finance

/s/
Milton Mesina
Economic Counsellor of the President

Technical Memorandum of Understanding

This Memorandum specifies the nature of the performance criteria and provides additional details on certain measures contained in the attached letter of intent.

1. The Central Bank shall conduct its foreign exchange transactions in the following manner: (a) all exchange transactions are to be carried out at the exchange rate determined freely by the market; (b) no additional foreign exchange surrender requirements beyond those in effect on January 31, 1985 shall be imposed; (c) the Central Bank shall buy foreign exchange (i) on its own account, to cover its own needs, including compliance with the net foreign assets targets in the program, and (ii) on account of the Government, to service the public sector foreign debt and to pay for oil imports; and (d) the Central Bank shall not intervene in the market for the purpose of influencing the exchange rate.

2. The proceeds of the temporary exchange taxes referred to in paragraph 15 of the letter of intent are to be credited to a special account in the Central Bank. This account is to be debited only to: (a) offset operating losses of the Central Bank; and (b) to compensate the Central Government and public entities for the additional cost arising as a result of the unification of the exchange system. At no time can the balance in the account be negative.

3. The stock of combined net credit of the Central Bank and the Banco de Reservas to the public sector, which was RD$1,739.2 million on September 30, 1984, is estimated to have been RD$1,802 million on December 31, 1984. Such credit shall not exceed RD$1,902 million on June 30, 1985 (performance criterion), and is projected not to exceed RD$1,852 million on September 30, 1985, and shall not exceed RD$1,802 million on December 31, 1985 (performance criterion) (Table 1). The aforementioned ceilings will be adjusted for any revisions to the outstanding stock as of December 31, 1984.

The combined net credit of the Central Bank and the Banco de Reservas to the public sector is defined as the sum of: (a) all forms of credit from the Central Bank and the Banco de Reservas to the Central Government, the decentralized and autonomous entities (with the exclusion of the Housing Bank), the CORDE enterprises for which the Government is a majority shareholder, Rosario Dominicana, and the oil refinery; minus (b) all deposits from the same institutions, excluding deposits in the Central Bank for the payment of external obligations for which a rescheduling is being sought.

4. On December 31, 1984 the sum of RD$45 million had been deposited in the Central Bank in respect of public sector debt service obligations falling due up to that date. The Central Bank will make the transfer in foreign exchange through a series of payments. Losses which the Central Bank may suffer as a result of these transfers will

be covered by the Central Government and the credit ceilings will be adjusted upward by these amounts. As of December 31, 1984 local currency deposits corresponding to other external debt obligations had not been made. During the review with the Fund (mentioned in paragraph 30 of the letter of intent) a schedule will be agreed for the liquidation of these obligations and the credit ceilings for the rest of the program period will take this into account. To the extent that debt relief is larger than envisaged, the credit ceilings and the net domestic assets ceiling will be adjusted downward accordingly.

5. The net domestic assets of the Central Bank will be subject to the following schedule in 1985: they will decline by no less than RD$50 million during the period January-June (performance criterion); and they are projected to decline by no less than RD$115 million during the period January-September and by no less than RD$165 million during the period January-December (Table 2).

The net domestic assets of the Central Bank are defined as the difference between the currency issued and net foreign assets. For the purpose of computing changes in net domestic assets, monthly changes in net foreign assets will be converted into pesos at an average of the rates at which transactions actually took place during the period (gross of the exchange taxes on exports).

6. The net foreign assets of the Central Bank, which were negative US$450.6 million on September 30, 1984, and were negative US$335.9 million on December 31, 1984 will not be less than negative US$300 million on June 30, 1985 (performance criterion); and are projected to be not less than negative US$279 million on September 30, 1985 and not less than negative US$227 million on December 31, 1985 (Table 3). Any reduction in foreign reserve liabilities through restructuring or refinancing will continue to be included as a reserve liability for purposes of this ceiling.

7. External payments arrears, including arrears to Paris Club creditors and commercial banks, estimated to have amounted to US$501 million on December 31, 1984, will be reduced through cash payments by at least US$64 million by June 30, 1985 (performance criterion); by at least US$74 million by September 30, 1985, and by at least US$89 million on December 31, 1985 (Table 4). No external payments arrears will be incurred at any time in 1985 (performance criterion). As part of the review with the Fund mentioned in paragraph 30 of the Letter of Intent, the authorities will reach understandings with the Fund on a schedule for the orderly elimination of those external arrears which will be outstanding on December 31, 1985.

8. The ceilings that shall apply through December 31, 1985 to disbursements under nonconcessional external public and publicly guaranteed debt are specified in Table 5.

Table 1. Dominican Republic: Quarterly Ceilings on Combined Central Bank and Reserve Bank Net Credit to the Public Sector 1/

(In millions of Dominican pesos)

	1984	1985			
	Dec. 31	Mar. 31	June 30 2/	Sept. 30 3/	Dec. 31 2/
Net credit to the public sector 4/	1,802	1,852	1,902	1,852	1,802

1/ The ceiling will be adjusted to reflect any revisions in the outstanding stock as of December 31, 1984.
2/ Performance criterion.
3/ Indicative ceiling.
4/ Excludes deposits relating to overdue external obligations (RD$45.2 million).

Table 2. Dominican Republic: Cumulative Reduction of Net Domestic Assets of the Central Bank, 1985 1/

(In millions of Dominican pesos)

	Outstanding Dec. 31, 1984	1985 Mar. 31	June 30 2/	Sept. 30 3/	Dec. 31 3/
Net domestic assets	1,632.2	100.0	-50.0	-114.9	-164.8

1/ Defined as the difference between the currency issued and the net foreign assets of the Central Bank (converted into pesos at an average of the rates at which transactions actually took place during the period--gross of the exchange taxes on exports). The exchange rate applied for the calculation of net foreign assets as of December 31, 1984 was RD$2.8=US$1.

2/ Performance criterion.

3/ Indicative ceiling.

Table 3. Dominican Republic: Quarterly Ceilings on Net Foreign Assets, 1985

(In millions of U.S. dollars)

	1984	1985			
	Dec. 31	Mar. 31	June 30 1/	Sept. 30 2/	Dec. 31 2/
Net foreign assets 3/	-335.9	-359.5	-300.0	-278.6	-227.2

1/ Performance criterion.
2/ Indicative ceiling.
3/ These numbers will be adjusted to the extent that collateral deposits are utilized to liquidate unpaid letters of credit.

Table 4. Dominican Republic: External Arrears, 1984-85

(In millions of U.S. dollars)

	Outstanding Dec. 31, 1984	Cumulative Cash Reduction in 1985		
		June 30	Sept. 30	Dec. 31
Arrears	501 1/	64 2/	74 3/	89 3/

1/ Excludes certain potential obligations that could arise from the Monetary Board's Resolution of May 10, 1984 and on which a decision has not been made as yet.
2/ Performance criterion.
3/ Indicative ceiling.

Table 5. Dominican Republic: Ceilings on Disbursements Under Nonconcessional External Public and Publicly Guaranteed Debt

(In millions of U.S. dollars)

Maturities (Years)	Disbursements During 1985 1/
0-1 year	-19.3 (net) 2/
Over 1 year, and no more than 12 years	198.5
Of which: Over 1 year, and no more than 5 years	64.2

1/ Excludes restructurings and/or refinancings.
2/ At no time during 1985 shall the cumulative disbursements exceed US$90.7 million, and there shall be net repayments of US$19.3 million during 1985.