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Dominica: 2005 Article IV Consultation, Fifth Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility and Requests for Waiver of Nonobservance of Performance Criterion, Financing Assurances Review, and Extension of Repurchase Expectations—Staff Report; and Public Information Notice and Press Release on the Executive Board Discussion

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of a combined discussion of the 2005Article IV consultation with Dominica and the fifth review under the three-year arrangement under the Poverty Reduction and Growth Facility and requests for a waiver of nonobservance of a performance criterion, financing assurances review, and extension of repurchase expectations, the following documents have been released and are included in this package:

- the staff report for the 2005 Article IV consultation, fifth review under the three-year arrangement under the Poverty Reduction and Growth Facility and requests for waiver of nonobservance of performance criterion, financing assurances review, and extension of repurchase expectations prepared by a staff team of the IMF, following discussions that ended on August 25, 2005, with the officials of Dominica on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on September 29, 2005. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- a Public Information Notice (PIN) and Press Release summarizing the views of the Executive Board as expressed during its October 14, 2005 discussion of the staff report that concluded the Article IV consultation, and the IMF arrangement, respectively.

The documents listed below have been or will be separately released.

Letter of Intent sent to the IMF by the authorities of Dominica*
Poverty Reduction Strategy Paper—Preparation Status Report
Statistical Appendix
Supplement Memorandum of Economic Policies by the authorities of Dominica*
Technical Memorandum of Understanding*
*May also be included in the Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to publicationpolicy@imf.org.

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INTERNATIONAL MONETARY FUND

DOMINICA

Staff Report for the 2005 Article IV Consultation, Fifth Review Under the Three-Year Arrangement Under the Poverty Reduction and Growth Facility and Requests for Waiver of Nonobservance of Performance Criterion, Financing Assurances Review, and Extension of Repurchase Expectations

Prepared by Western Hemisphere Department
(In consultation with other departments)

Approved by José Fajgenbaum and Matthew Fisher

September 29, 2005

- **Recent developments:** The economy is recovering from the aftermath of an economic and financial crisis in 2001–02 when output contracted by some 10 percent. The roots of the crisis lay in an unsustainable build-up of public debt in the late 1990s. The build-up in domestic arrears that this prompted, coupled with the adverse effects of a severe drought on agriculture and a decline in the nascent tourism sector following the September 11 attacks, triggered a steep recession. The strong fiscal adjustment and collaborative debt restructuring that the authorities subsequently put in place have been accompanied by a rebound in output. The economy is set to register its second year of above average growth in 2005.

- **Arrangement.** A three-year Poverty Reduction and Growth Facility (PRGF) arrangement of SDR 7.7 million (94 percent of quota) was approved on December 29, 2003. The last program review was completed on March 7, 2005, and a total of SDR 4.2 million has so far been disbursed. Program implementation remains strong, with all but one quantitative performance criteria observed. Progress at structural reforms have been somewhat slower than envisaged, but remains satisfactory. In the attached supplementary memorandum of economic policies, the authorities outline their reform program for 2005/06 and request completion of the fifth review.

- **Exchange regime.** Dominica is a member of the Eastern Caribbean Currency Union (ECCU), which is administered by the Eastern Caribbean Central Bank (ECCB). The common currency, the Eastern Caribbean dollar, has been pegged to the U.S. dollar since July 1976 at US$1=EC$2.70. Dominica has accepted the obligations of Article VIII, Sections 2, 3 and 4, and maintains an exchange system that is free of restrictions on the making of payments and transfers for current international transactions.

- **Fund Relations.** The last Article IV consultation was concluded in August 2002, and the Public Information Notice (PIN) summarizing the Executive Directors' views and policy recommendations is available on the IMF's public website at: http://www.imf.org/external/np/sec/pn/2002/pn02116.htm

- **Missions:** Two missions visited Roseau. The first during June 9–23, 2005, comprising Messrs. Panth (Head), Dyczewski, Njoroge, Rasmussen (all WHD), Selassie, Rodriguez (both PDR). Mr. Graham (World Bank) and representatives from the ECCB and the Caribbean Development Bank participated in the mission. Mr. Campbell (OED) and Ms. Sahay (WHD) joined the mission for the final discussions. A second mission visited Roseau during August 22–26, 2005 to conclude the discussions, comprising Messrs. Selassie (Head), Njoroge, Rasmussen (all WHD) and Rodriguez (PDR).

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EXECUTIVE SUMMARY

- **Dominica is recovering from the aftermath of an economic and financial crisis in 2001–02 when output contracted by 10 percent**. With a rebound in economic growth, strong fiscal consolidation, and a collaborative debt restructuring agreement, public finances are now on a firmer footing. Playing off the recovery, the incumbent administration won another five-year term in the May 2005 general elections.

- **The 2001–02 crisis originated in the expansionary fiscal policies of the preceding decade, when the authorities sought to prop-up activity by increasing public spending.** By 2001, this approach had reached its limits and the government faced a liquidity crisis. Coupled with the adverse effects of a severe drought and the September 2001 terrorist attacks, the result was a steep recession.

- **The authorities' reform strategy has since mid-2003 aimed at ensuring an orderly adjustment, followed by measures to reinvigorate growth.** With the debt-to-GDP ratio approaching 130 percent, the authorities concluded in December 2003 that the debt situation was unsustainable and launched a debt exchange offer. The Fund has supported the authorities' reforms since 2002 initially through a Stand-By Arrangement (SBA) and since end-2003 through a PRGF arrangement.

- **The strategy has been remarkably successful.** Economic growth has increased to over 3 percent a year. The central government primary balance has swung to a surplus of 4½ percent of GDP in 2004/05, with both higher revenues and lower spending contributing to the improvement. The debt restructuring process coupled with the fiscal consolidation effort allowed the debt stock to decline to 117 percent of GDP at end-2004.

- **Program implementation has been solid and staff recommends completion of the financing assurances review.** All end-June quantitative performance criteria were met, most with large margins, although the continuous performance criterion on external arrears was missed. All three structural benchmarks for the fifth review have been broadly completed, and legislation to introduce a VAT was recently passed by Parliament. Progress on structural reforms has generally been slower than hoped, reflecting limited implementation capacity and difficulties in building consensus.

- **More work is required to conclude the debt restructuring process**. Agreements have been reached with creditors holding about 70 percent of the debt eligible for restructuring. Discussions with nonparticipating creditors continue and the authorities are depositing interest payments into an escrow account under the restructured terms. The issuance of new bonds to all participating creditors has, however, yet to be completed.

- **The critical challenge now is sustaining the current growth momentum.** Ensuring progress in lowering poverty and unemployment will require decisive action. Challenges include the poor prospects for the banana sector, rising oil prices, a high vulnerability to natural disasters, the continued high debt level and the large unfunded liabilities in the social security system, and structural rigidities. Consistent with the increased focus on growth, the authorities' program for 2005/06 has a stronger emphasis on structural reforms, with the forthcoming Growth and Social Protection Strategy document representing an important step forward.

I. Introduction

1. **Dominica has come a long way from the low-point of the 2001–02 economic crisis when output contracted by 10 percent**. Economic growth has recovered more recently and is set to record the second straight year of above average growth in 2005. Reflecting strong fiscal consolidation and a collaborative debt restructuring agreement, public finances are now on a firmer footing. The structure and transparency of public finances is also improving.

2. **Playing off the recovery, the incumbent administration won another five-year term in the May 2005 general elections**. The Dominica Labor Party (DLP) was returned to Parliament with an increased majority. The opposition campaigned vocally against the Fund-supported program.

3. **The critical challenge for the authorities now is sustaining the current growth momentum.** While Dominica has been at the forefront in addressing the fiscal challenges that most of the countries in the region face,[1] it has yet to tackle the constraints on growth. Like other countries in the region, sustained private sector-led growth has proved elusive in Dominica, and prospects for maintaining growth at current levels remain uncertain. Structural rigidities abound in the economy and, without decisive action to address these bottlenecks, progress in lowering poverty and unemployment (Box 1) will be constrained.

Box 1. Social Indicators

In a regional perspective, Dominica has a per capita income at the lower end among the Eastern Caribbean Currency Union (ECCU) countries but relatively high social indicators. The economy is highly dependent on agriculture (banana) with manufacturing and tourism playing a lesser role.

Table 1. Social Indicators

	GDP per Capita (US$)	Human Development Index Ranking 1/	Life Expectancy at Birth	Voice and Accountability 2/	Poverty Rate
Caribbean	5,366	78	69	68	28
ECCU	5,633	73	72	74	27
Non-ECCU	5,189	81	68	65	29
Dominica	**3,554**	**95**	**73**	**81**	**33**

Source: World Bank.

1/ Out of 174 countries.
2/ Percentile ranking.

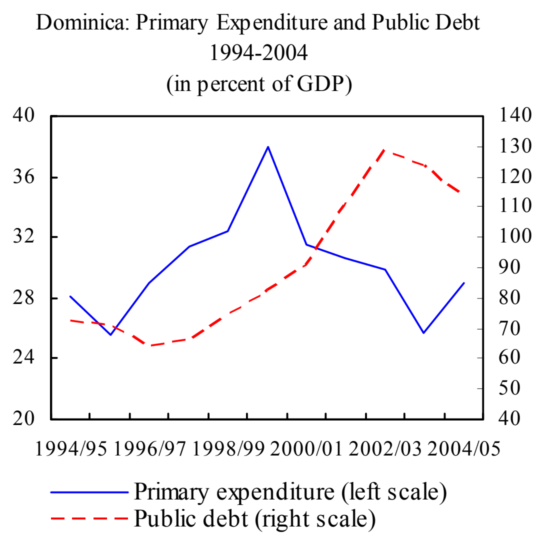
4. **The Fund has supported the authorities' reforms since 2002 initially through a Stand-By Arrangement (SBA) and since end-2003 through a PRGF arrangement**. Program implementation since the introduction of the PRGF has been solid. In the attached letter of intent and supplementary memorandum of economic policies (MEP), the authorities

[1] See *Eastern Caribbean Currency Union—Report for the 2005 Regional Discussions*, IMF Country Report No. 05/304.

outline their economic policies for the coming months and request a waiver for the nonobservance of a performance criterion for completion of the fifth review under the PRGF.

II. Background and Perspective

5. **The roots of the 2001–02 economic crisis lie in the expansionary fiscal policies of the preceding decade**. As output growth declined in the 1990s, the authorities sought to prop-up activity by increasing public spending. The primary balance of the central government turned strongly negative in the mid-1990s, and public debt quickly reached unsustainable levels (Figure 1). By 2001, this approach had reached its limits. With financing only available at precipitously high interest rates, the newly elected DLP government faced a major liquidity crisis. The build-up in domestic arrears that ensued, coupled with the adverse effects of a severe drought on agriculture and the September 2001 terrorist attacks on the nascent tourism sector, precipitated a steep recession.



6. **Dominica's recent growth performance has been much weaker than the other ECCU countries**. While output growth in Dominica kept pace with its brethren in the 1980s, the situation reverses for much of the 1990s. Dominica also experienced the sharpest recession following the September 11 attacks. What explains this difference?

- **The dominant role of agriculture**. Agriculture (banana production, in particular) plays a much larger role in Dominica than in the other ECCU countries, and the 1990s were a relatively difficult time for the sector. Reflecting the uncertainty regarding the future of the preferential trade arrangements for bananas, a trend decline in the banana export price, and the higher productivity of other producers, acreage, employment and investment in the sector has been declining since the early 1990s.

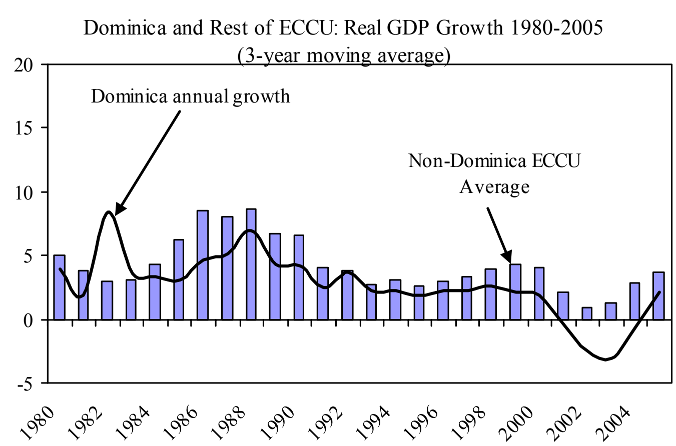
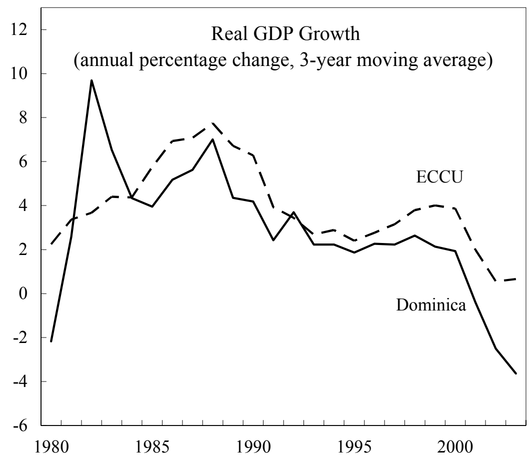


Figure 1. Dominica: Emergence of the Crisis

The growth slowdown was regional.

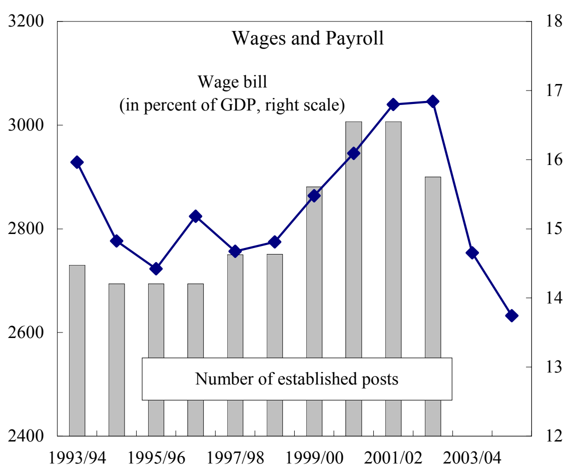


As growth slowed in the 1990s...

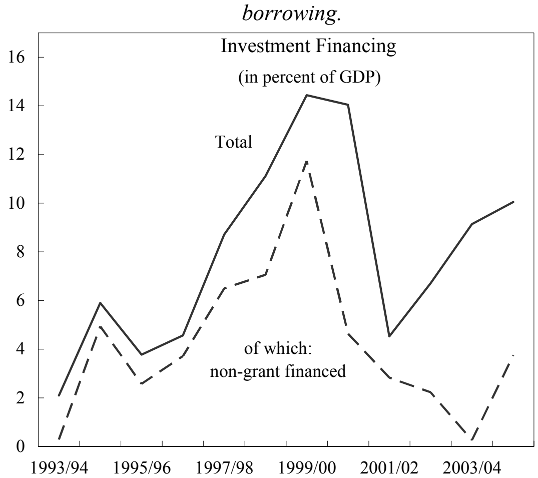
Sectoral contribution to real GDP growth

	1986-90	1991-95	1996-00	2001-02	2003-04
	(annual percentage change)				
Real GDP Growth	5.2	2.1	2.2	-4.4	1.7
Bananas	0.8	-0.6	-0.1	-0.6	-0.2
Government Services	0.4	0.1	0.5	0.8	-0.6
Manuf/Constr/Trade	1.8	1.0	0.6	-1.9	1.1
Other	2.2	1.6	1.2	-2.7	1.5

... the government payroll expanded dramatically in the second half of the 1990s...



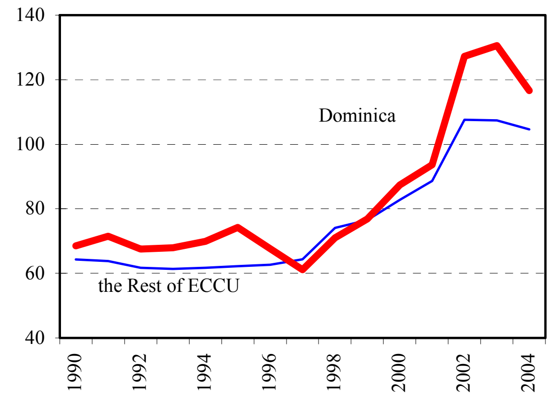
...as did government investment financed by borrowing.



Sources: Dominican authorities; and Fund staff estimates.

- **Agricultural difficulties were compounded by the government's liquidity constraints in 2001–02**. While the other ECCU countries also attempted to counteract the 1990s growth slowdown through expansionary fiscal policies, only in Dominica did the liquidity constraint become binding. This seems to reflect concerns about the country's growth prospects. With few beaches at hand, the scope to diversify economic activity away from agriculture to traditional tourism activities as in the other neighboring islands was limited.

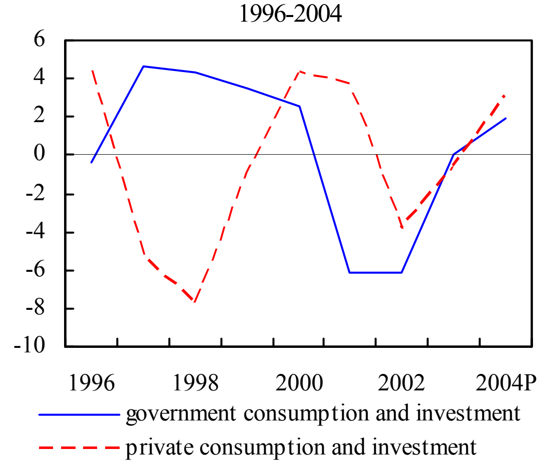
Dominica and the Rest of ECCU: Public Debt 1990-2004



- **Migration**. With per capita income at the low-end in the region, emigration (and consequent loss of human capital) from Dominica has not just been to the OECD countries but also to the richer countries in the region.

7. **As government arrears mounted, macroeconomic policies could do little to counter the 2001–02 recession**. The downturn also weakened revenue collection, causing the primary balance to swing more sharply into deficit (8½ percent of GDP in 1999/00). After peaking at 38 percent of GDP in 1999/00, public spending was reduced sharply in face of financing constraints contributing to the drop in output. The arrears that the government accumulated to the domestic private sector also caused private demand to decline. Monetary policy, conducted at the regional level, remained largely passive.

Dominica: Contribution to Real GDP Growth 1996-2004



8. **The stabilization program (supported by a SBA) introduced in the 2002/03 budget soon fizzled due to weaker than expected economic conditions and policy slippages**. Economic growth in 2002 was much weaker (-4½ percent) than envisaged under the SBA (-½ percent), reflecting lower exports and tourism receipts, as well as an unforeseen sharp decline in private and public investment (the latter due to slow implementation of the public sector investment program). Despite higher foreign grants and lower capital spending, the overall deficit target for 2002/03 was 1½ percent of GDP worse than budgeted because of cyclical factors and the failure to hold down the wage bill as envisaged. With little progress on the fiscal front, arrears to private creditors continued to accumulate.

9. **The more focused and comprehensive adjustment strategy adopted in mid-2003 enabled the economy to emerge from the crisis** (Box 2). This revised strategy—initially supported by the SBA and a PRGF since December 2003—focused first on prospects for an orderly adjustment, followed by measures to reinvigorate growth and a debt strategy to ensure medium-term fiscal sustainability. The strategy has been remarkably successful, allowing growth in 2004–05 to converge to the ECCU regional average:

- **Fiscal consolidation**. A central government primary balance of 3 percent of GDP was established as the objective for budgetary policies in due course. In the event, the primary balance has swung from an average deficit of 1½–2 percent of GDP in 2001–03 to a surplus of 4½ percent of GDP in 2004/05 (about 4 percent of GDP excluding one-off factors). Both higher revenues and lower spending contributed to the improvement. Revenue measures aimed at broadening the tax base and improving the efficiency of the tax system, and the economic recovery also helped to increase the revenue to GDP ratio. On the expenditure side, the government has shown remarkable restraint. The wage bill, which at 17 percent of GDP was one of the largest in the region, has been reduced by more than 3 percentage points. Nongrant funded investment spending has also been scaled back.

- **Debt restructuring**. With the debt-to-GDP ratio approaching 130 percent, the authorities concluded in December 2003 that the debt situation was unsustainable, an assessment supported by the staff. The debt exchange offer that the authorities eventually launched was aimed primarily (but not exclusively) at private sector creditors.[2] The restructuring process coupled with the fiscal consolidation effort has allowed the debt stock to decline to 117 percent of GDP at end-2004.

- **Structural fiscal reforms**. A broad range of structural reforms have been initiated, though only a few have come to fruition. Most notably, legislation to introduce a VAT was recently passed by Parliament. Progress on other fronts has, however, been slower than hoped. In the main, this reflects the very limited implementation capacity, including from the government's inability to build consensus in some areas.

[2] Claims issued prior to December 2003 were to be exchanged for three new local currency denominated bonds carrying a coupon rate of 3.5 percent. These bonds have 10, 20 and 30-year maturities, and entail principal reductions of 30, 20, and 0 percent, respectively.

Box 2. Past Staff Advice

The authorities feel that previous staff advice has been broadly useful …

They noted that despite limited appetite for Fund-supported programs in the region and harsh criticism at home, they had sought Fund advice and support for their economic program. Moreover, the policies that have been pursued have paid off as evidenced by the quick resumption of growth.

but with a couple of caveats:

First, officials wondered if the Fund should not have been more candid about the large expensively financed spending increases in the late 1990s. For instance, they noted that staff statements had on one occasion referred to these spending plans as being "ambitious." This was used in public debates by the then administration, as a validation of its economic strategy.

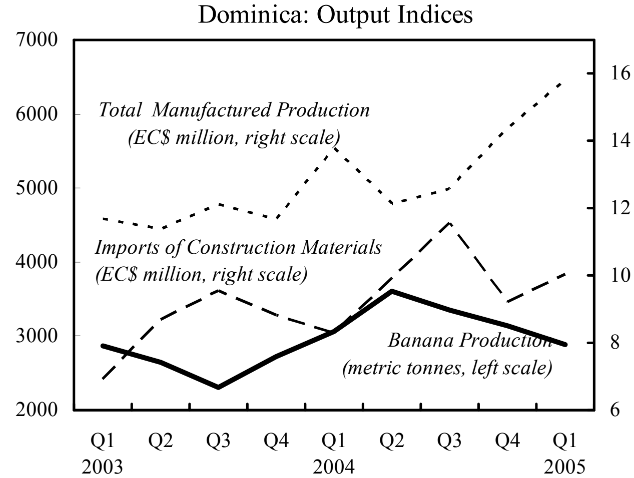
Second, the authorities thought that the Fund had at times not been cognizant enough of Dominica's limited capacity to implement structural reforms.

III. Recent Developments and Performance under the Program

10. **Recent economic developments have been favorable**:

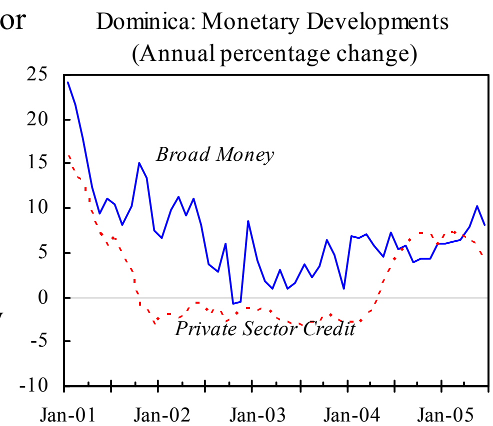
- **Economic growth has resumed and inflation remains subdued**. Real GDP increased in 2004 by an estimated 3.5 percent. The expansion was relatively broad based, with virtually all sectors showing a pick-up. The expansion has continued and staff and the authorities expect real GDP growth to reach 3 percent in 2005 (albeit subject to downside risks). Inflation declined in 2004 and has remained subdued through July 2005, despite the pass through of higher energy prices to consumers.

Dominica: Output Indices

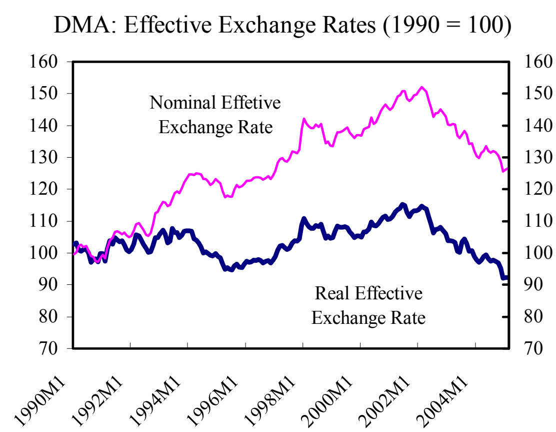


- **Mirroring the domestic recovery, import growth has picked up**. Increased tourism receipts however ameliorated the current account impact, with merchandise exports broadly unchanged.[3]

- **Financial intermediation has also rebounded** (Table 4). After a contraction that started in mid-2001, credit to the private sector turned positive from mid-2004. Notwithstanding the pick-up in credit growth, banking system liquidity remains high due, in part, to the strengthened fiscal accounts and also growing deposits. Banks have used this opportunity to increase their net foreign asset position in recent months. The debt restructuring (by design) had a very limited effect on banks' balance sheets. Moreover, indicators of banking system soundness suggest a modest reduction in nonperforming loans.



- **The East Caribbean dollar, which is pegged to the U.S. dollar, has depreciated markedly in real effective exchange rate (REER) terms since 2002**. Mirroring the U.S. dollar, the E.C. dollar depreciated in real effective terms by 7 percent in 2004 and by a further 3½ percent through mid-2005. The continuing rapid growth in tourism and related activities are suggestive of competitiveness being adequate.[4]



11. **Performance relative to the program targets has been solid**.

- **All end-June quantitative performance criteria were met, most with large margins** (Table 5). The continuous performance criterion on the nonaccumulation of external arrears was, however, missed due to a brief delay in servicing a government guaranteed loan.

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[3] The first round effect of higher oil prices on imports in 2005 is estimated to be about 2 percentage points of GDP, although this is set to be partially offset by endogenous changes, including lower oil demand.

[4] See P. Cashin, P. Njoroge, and P. Rodriguez (2004), *Competitiveness in the ECCU: Measures of the Real Exchange Rate*, ECCU Selected Issues, IMF Country Report No. 04/335.

- **Fiscal performance in FY 2004/05 was strong**. Revenue collection was almost 2 percentage points of GDP higher than previously projected, reflecting arrears collection and windfall gains.[5] Current expenditures exceeded the baseline program target, but this was mainly on account of an unbudgeted transfer of ¾ percent of GDP required for the establishment of the regional Caribbean Court of Justice (CCJ). At the same time, delays in project execution and donor disbursement saw significant shortfalls in capital spending. At 4½ percent of GDP (4 percent excluding the one-offs from migrants deposits and the CCJ payment), the primary surplus for the year was 2½ percentage points of GDP higher than programmed.

Dominica: Recent Fiscal Performance

	2003/04		2004/05	
	Prog.	Actual	Prog. 3/	Actual
	(in percent of period GDP)			
Primary balance 1/	**1.7**	**5.6**	**2.0**	**4.4**
Revenues (excl. grants)	**29.5**	**31.2**	**31.3**	**33.1**
Non-Interest Expenditures and Other	**-27.9**	**-25.6**	**-29.3**	**-28.8**
Non-interest current expenditures	-26.8	-25.4	-24.7	-25.3
Investment (net of grants) and other 2/	-1.1	-0.2	-4.6	-3.5
Memorandum item:				
Grants	7.4	8.8	8.1	5.9
Non grant-financed investment (ratio)	32	29	39	41

1/ Measured from below the line.
2/ Includes net lending and statistical discrepancy.
3/ IMF Country Report No. 05/117.

12. **There has been encouraging progress on structural reforms** (MEP ¶5).

- All three structural benchmarks for the fifth review have been broadly completed (Table 6), although the proposals to amend the Finance Administration Act were finalized without numerical targets.

- The government has decided to publish in the Official Gazette all Cabinet decisions granting new tax and duty concessions, identifying the beneficiary as well as its legal basis—a step that will enhance the transparency of public finances.

- With parliamentary approval of the VAT and excise tax legislations, substantial progress has been made towards the introduction of a VAT on March 1, 2006.

13. **More work is required to conclude the debt restructuring process**. As reported previously (IMF Country Report No. 05/117), agreements have been reached with creditors holding just above 70 percent of the debt eligible for restructuring. Discussions with three creditors that account for the bulk of the remaining unrestructured debt are continuing. However, staff understands that one of these creditors, the Exim Bank of Taiwan Province of China, recently filed suit in a New York District Court to recover its claim (about US$12 million). Given that the court case has just been initiated, its implications on Dominica's

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[5] The fiscal accounts benefited from some 1 percent of GDP in migrants' deposits—proceeds required of regional migrants, and forfeited when they fail to return to their country of origin. The fees were introduced to stem the flow of migrants using Dominica as a transit point to neighboring French territories. The government has further tightened travel restrictions in recent months, and now requires most such travelers to obtain a visa to travel to Dominica.

ability to reach collaborative agreement with this creditor and on program implementation remain uncertain. Staff will review documents as they become available and will monitor developments closely. As a sign of good faith toward nonparticipating creditors, the authorities have continued to deposit into an escrow account interest accrued under the original terms until the date the exchange offer was closed, and under the restructured terms subsequently.

IV. Report on the Discussions

14. **The Article IV consultation and program discussions took place against the backdrop of a broadly favorable economic environment, but with concerns about its medium-term viability and the need to reduce poverty**. Notwithstanding the recent gains, the authorities acknowledged that much remains to be done to sustain the current growth momentum—which is essential for the government's central objectives: job creation and poverty alleviation. The government's strategy document to address these objectives—the Growth and Social Protection Strategy—is currently being finalized. The authorities reiterated their commitment to prudent fiscal policies, accelerating structural reforms and reducing vulnerability to shocks. Against this background, the policy and program discussions focused on:

- **Sustaining the current growth momentum**. The government recognized the large role that temporary factors (including favorable agriculture conditions in 2004) have played in the recent upturn. The discussions therefore focused on how best to remove policy-induced distortions that might impede private investment.

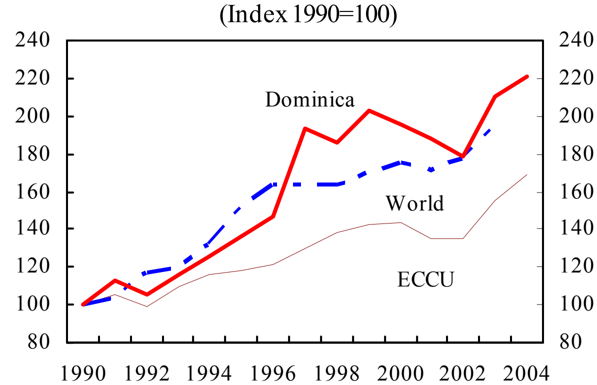
- **Putting public finances on a sustainable footing**. With the 2004/05 primary balance having reached the level targeted for gradually reversing the debt build-up of recent years, discussions focused on measures required to ensure the long-term viability of public finances. The scope and options for accelerating many of the structural fiscal reforms under the program was also considered.

- **Reducing vulnerability to shocks**. Discussions on Dominica's vulnerability to natural disasters were put sharply into focus by the earthquake that hit the north of the island last November, causing damage estimated at 7 percent of GDP. The risks that the limited oversight of the domestic financial sector poses were also considered.

A. Outlook

15. **Staff and the authorities worked together to update the medium term macroeconomic framework** (Table 7). There was broad agreement that annual GDP growth of some 3 percent should be feasible over the medium term (Box 3), and that annual inflation would remain subdued at below 2 percent. The external current account is expected to improve over the medium term. Strong growth in tourism receipts should continue in the near term—particularly in view of the recent expansion of hotel room capacity—and merchandise exports (of niche agricultural products) are expected to strengthen in the outer years. Import growth, after rising sharply this year, reflecting higher private and public investment, is expected to slow somewhat.

Dominica: Tourism Receipts
(Index 1990=100)



Source: World Tourism Organization and Caribbean Tourism Organization.

Box 3. Dominica: Growth Performance and Potential

Dominica's growth potential is better than recent experience would imply and macroeconomic policies remain key to achieving higher growth.

- Simple simulations show that, given its endowments, Dominica is **performing below its growth potential.** Barro (1991) uses variations in initial per capita income, human capital and government consumption to explain growth rates across a wide number of countries.[1/] Levine and Renelt (2002) use, in addition, investment and population increase as other growth determinants. These equations predict per capita income growth for Dominica in the range of 2¾–6 percent. Even at the conservative end, the realized rate, during 1990−2003, of about 1½ percent compares unfavorably.[2/]
- Reducing government size and increasing trade can significantly improve performance. A World Bank cross-Caribbean econometric study suggests that if policy trends in the 1990s had persisted, Dominica's annual growth would be even lower—with the increasing inward orientation of the economy and upward movement in government consumption more than offsetting the impact of increased education, financial deepening, and stronger public infrastructure.[3/] Critically, this same study finds that if instead, Dominica's government consumption burden decreased to the 75th percentile ranking in the Latin America and Caribbean region, annual real GDP growth could jump to 2.9 percent.

1/ R. J. Barro, (1991). *Economic Growth in a Cross-Section of Countries. Quarterly Journal of Economics, Vol. 106, pp. 407−443.*

2/ R. Levine, and D. Renelt (1992). *A Sensitivity Analysis of Cross-Country Growth Regressions, American Economic Review, Vol. 82, pp. 942−63.*

3/ World Bank. *A time to Choose: Caribbean Development in the 21st Century. 2005.*

16. **Considerable uncertainty attaches to this scenario**.

- On the positive side, Dominica's forested volcanic topography and underwater attractions render it well placed to exploit the fast growing global adventure and nature-based tourism. The considerable potential to export geothermal-based electricity to the neighboring French territories of Guadeloupe and Martinique, if realized, could boost output significantly.

- On the other hand, downside risks are nontrivial. Prospects for the banana sector remain grim, particularly in light of the EU's recently announced plans for reforming its import arrangements. Despite shrinking considerably in the past decade, the sector continues to employ a large number of farmers. However, some observers, particularly the representatives of the banana sector, believe that the sector can rebound. The recent rise in oil prices—which have been passed on in full to consumers, but at times with a short delay—and their potential to dampen private consumption also heighten downside risks, particularly in the near term. Dominica's high vulnerability to natural disasters and its high debt (notwithstanding the debt restructuring) are major risks.

B. Reinvigorating Growth and Reducing Poverty

17. **The authorities stressed their desire to see the private sector play a dominant role in the economy**. They acknowledged that, despite past high levels of public investment, growth prospects had failed to improve and unemployment and poverty remain high—at 25 percent of the labor force and 33 percent of the population, respectively, as of 2002. Staff concurred with this assessment, noting that investment in infrastructure in the past had been neither well-considered (often projects were left incomplete) nor affordable (financed nonconcessionally). The significant loss of human capital through migration had further undermined growth potential. Against this backdrop, staff and the authorities agreed on the need for policies to facilitate a shift away from the public sector driven growth and employment, in favor of the private sector. These include, removing policy-induced bottlenecks (see below) to allow emerging sectors to flourish, better prioritizing public sector investment, and improving the private sector investment climate.

18. **There was broad agreement that, at its current level, the real exchange rate would not hamper growth prospects**. The U.S. dollar's depreciation since 2002 has allowed CPI-based REER to revert to pre-1990s levels, giving competitiveness a positive fillip. The authorities were satisfied that any misalignment of the E.C. dollar had been eliminated by this depreciation. They considered that the recent focus on niche markets where the country had a comparative advantage, such as adventure tourism and high value added agricultural products, would be beneficial given that wages in Dominica were not particularly low. Tourism industry representatives noted an urgent need for better training and infrastructure development, but otherwise felt that the sector was reasonably competitive. Other business community representatives stressed the high cost of electricity and shipping, and a slow and unnecessarily bureaucratic investment approval process. The

authorities noted that both the high cost of electricity and the investment approval process are going to be addressed in the coming months.

19. **The mission stressed the need to address bottlenecks to investment—some of which are being tackled as part of the PRGF-supported program**.

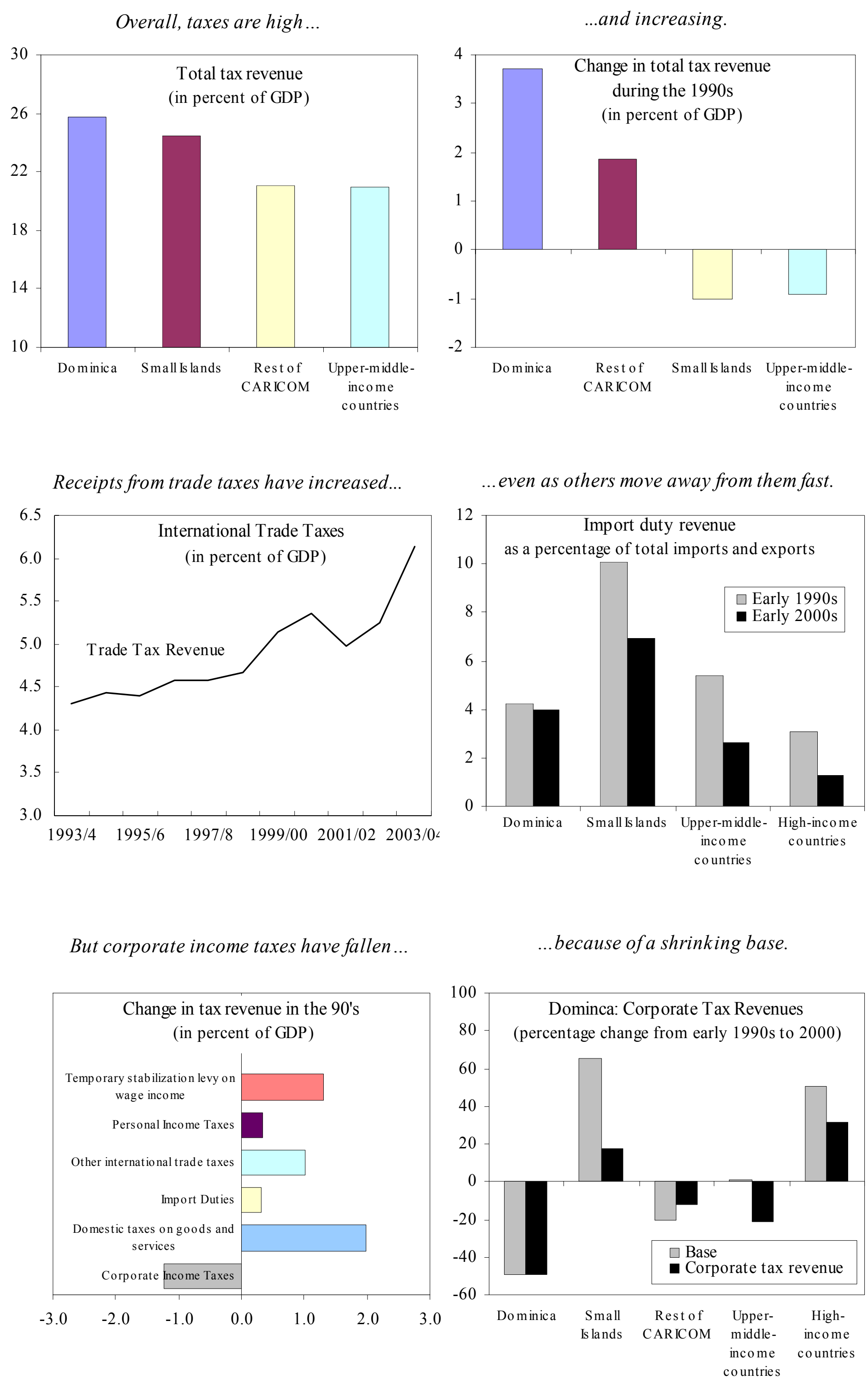
- The privately-owned electricity company, DOMLEC, currently has monopoly rights for electricity generation, transmission and distribution. Staff therefore emphasized the need to revamp the legislative framework governing the electricity sector to allow new entrants, including to tap the country's considerable geothermal potential. The envisaged reforms, which the authorities would like to put in place by the end of this year (MEP ¶10), will establish a regulatory commission and institute a tariff structure more reflective of production costs.

- The public sector agencies engaged in investment promotion—Dominica Export Import Agency (DEXIA), the National Development Cooperation (NDC) and AID Bank—also need to be reviewed. The mission questioned the need for three institutions, as well as their effectiveness in promoting investment and limited accountability. DEXIA's monopoly on rice and sugar importation is questionable given the desire for the private sector to play the dominant role in the economy. NDC's investment approval process is slow and uncertain, and the agency fails to operate as a "one-stop" investment promotion agency. The AID Bank's balance sheet needs closer scrutiny. The authorities are of the view that all three institutions had a role to play in the economy, but acknowledged that their operations may need streamlining. To that end, they agreed to undertake strategic reviews of all three institutions and establish implementation action plans by end-December 2005 (MEP ¶10).

- The mission also pointed to the absence of a national cadastral survey, and land registration is neither mandatory nor comprehensive, often making it difficult to establish ownership unambiguously and to use land as collateral for borrowing. The mission urged the authorities to accelerate the program to modernize land registration.

20. **There was extensive discussion on the merits of tax incentives to promote investment**. Staff argued that incentives are costly (forgone customs revenue in 2004/05 are estimated at about 4½ percentage points of GDP), administratively burdensome, and nontransparent (Figure 2). Moreover, policies that seek to identify and support winners are likely to create a cycle of dependency that sustains uncompetitive firms. The authorities argued that competition between regional economies generates considerable pressure for granting tax incentives for new investments. The government also thought the costs identified by staff were somewhat exaggerated given that the imports may have never have existed as a revenue source in the absence of the tax concessions. The mission nonetheless

Figure 2. Dominica: Tax Structure



Source: Keen and Simone (2004) and Fund Staff calculations.

noted that the concessions' benefits in terms of increased FDI appear to have been limited. Further, a recent World Bank survey of firms operating in the ECCU region suggests that investors attach a relatively low weight to fiscal incentives in determining investment location. Staff recommended adopting a regional cooperative approach in reducing statutory concessions. The authorities agreed to undertake a comprehensive review of statutory exemptions (MEP ¶20) and keep to a minimum recourse to discretionary tax exemptions—which has been increasing lately.

21. **The authorities intend to strengthen policies on education and migration**. The loss of a substantial number of nurses in recent years, to the U.S. and U.K., in particular, has strained local medical services delivery. The authorities saw scope for expanding the training of nurses in the near term, perhaps with private-sector interest, to a full-fledged export sector. Staff saw merit in this initiative, but noted the need to limit the budgetary implications by obtaining full cost recovery. The authorities were also keen to increase remittances and investment from Dominica's Diaspora to offset the 'brain drain.' They noted that initial steps had already been taken towards defining such a policy by commissioning a report by Dominicans in the Diaspora on how best the government can facilitate these activities.

C. Fiscal Policy and Debt Sustainability

Medium-term context

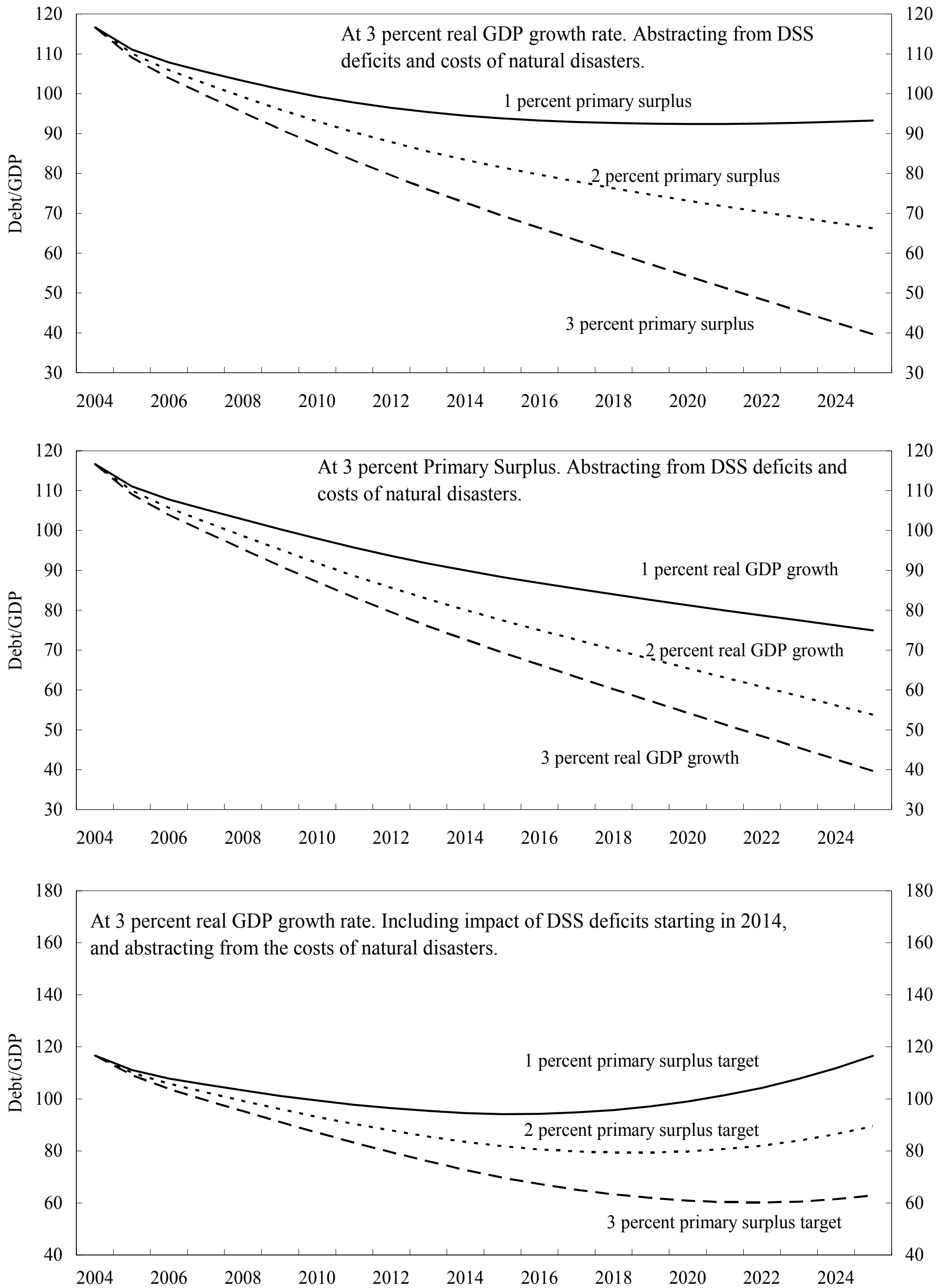
22. **Discussions on the FY 2005/06 budget were preceded by a comprehensive assessment of the medium-term fiscal outlook**.[6] The debt sustainability analysis discussed with the authorities affirms that the 3 percent of GDP central government primary surplus being targeted under the program would ensure a gradual decline in debt, provided growth remains at current levels and Dominica Social Security's (DSS) finances are improved.[7] Staff highlighted the sensitivity of the public debt path to both the assumed primary surplus and the economic growth rate.[8] Abstracting from DSS deficits, if a primary surplus of just 2 percent of GDP were to be targeted, the debt to GDP ratio would remain above 80 percent through 2015 (Figure 3). In the same vein, an average growth performance of 1–2 percent during the projection period would result in a similar very gradual decline in public debt (Figure 3). In both cases, the inclusion of DSS deficits projected under current policies would

[6] The medium-term primary balance objective under the program was initially based on growth remaining at the historical average of 2 percent per year, but it did not take into account the projected deficits of the social security system (see below).

[7] Under the baseline scenario, debt would decline to 60 percent in 2018. The fiscal benchmarks approved by the ECCB's Monetary Council call for this target to be achieved by 2007.

[8] The analysis assumes that nonparticipating creditors agree to participate in the debt restructuring process.

Figure 3. Dominica: Public Sector Debt Dynamics After Restructuring



Source: Country authorities and Fund staff estimates.

put the debt path back on an unsustainable trajectory (Figure 3). The authorities agreed that there were two options to avoid such an outcome: a primary balance target above 3 percent or adjusting the parameters of the social security system to eliminate DSS deficits. They saw merit in addressing these deficits through reforms (see below) rather than targeting a permanently higher primary surplus. The mission supported this approach.

FY 2005/06 budget

23. **Despite its mildly expansionary stance, the FY 2005/06 budget is consistent with further debt consolidation (MEP ¶11–13).** Based on relatively conservative revenue estimates, the authorities' budget targets a central government primary surplus of 3 percent of GDP to help reduce the debt burden.[9] The improved fiscal outlook and projected increase in grants has created room to increase capital expenditure to address, among others, the much needed road repairs required following last year's earthquake. Current expenditure will remain contained, with noninterest outlays held constant in real terms and the wage bill broadly unchanged as a ratio to GDP. By prioritizing capital projects within a tight overall expenditure envelope, the budget aims to support growth.

24. **The mission welcomed the budget, but noted that adhering to the wage bill target would require complementary reforms**. The authorities restored the 5 percent cut in public sector wages introduced in the 2003/04 budget. Staff supported this initiative, but regretted that delays in identifying and reducing excessive public sector employment as envisaged under the program will preclude a reduction in the wage bill to GDP ratio. The authorities stressed their commitment to a smaller, more efficient and better paid public service. Moreover, they intend to reduce the wage bill by 1–1½ percentage points of GDP over the medium term from its current level of 13¾ percent of GDP (MEP ¶16). This target will be realized principally through streamlining, commercializing or privatizing nonessential services.[10] To ensure adherence to the budgeted wage bill ceiling in 2005/06, the government has initiated steps to outsource janitorial and government building security services as well as streamlining the airports and ports authorities (MEP ¶16).

25. **Staff noted that effective implementation of the public sector investment program (PSIP) will be a major challenge given its size and capacity constraints**. The sectoral composition of the PSIP could be brought more in line with the government's growth strategy by focusing on investments in human and physical capital. Monitoring and planning of the PSIP could be strengthened by prioritizing projects in a comprehensive multi-year rolling framework, and sequencing in line with institutional capacity and the flow

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[9] Under the program, any additional revenue from migrants' deposits will not count towards the primary balance target, but go towards reducing debt.

[10] A preliminary review by the ministry of finance has shown scope for reducing the wage bill by as much as 1 percentage point of GDP.

of funds. The authorities noted that greater flexibility in the use of grant funds from donors would improve PSIP execution.

Dominica Social Security

26. **The authorities and staff agreed that a key priority will be addressing precarious DSS finances**. A recent FAD/World Bank technical assistance mission confirmed that, as the pension system matures and the ratio of contributors declines, DSS will start to run deficits (by about 2014) and eventually deplete its reserves (by about 2025). The system's unfunded liabilities are estimated at some 150 percent of 2004 GDP and represent a major threat to public finances. Adjustments that need to be considered to address this risk include: a gradual reduction in benefits; raising the statutory retirement age; increasing the contribution rate; and diversifying the investment portfolio. Staff stressed that the early initiation of reforms could help avoid abrupt and drastic changes later. The authorities acknowledged the need for reform, and have undertaken to review reform options in a timely way (MEP ¶15).

Other fiscal pressure points

27. **The institutional setting for fiscal policy needs further strengthening**. The priorities in the areas of budgetary planning and implementation include:

- **Fiscal Responsibility Law**. The authorities intend to institutionalize fiscal discipline over the medium term, and discussed with the mission their plans to amend the existing Finance Administration Act (FAA) (MEP ¶17). This would set legal guidelines with broad objectives for the primary balance and budgetary design procedures. Work is already at an advanced stage, but the authorities stressed the need for wider public consultation and awareness before these amendments can be finalized.

- **Strengthening public expenditure management**. Progress is being made, especially in reconciling bank accounts, and improving the coverage, reporting and monitoring of expenditures. All government bank accounts are now captured in the general ledger. However, further work is needed to establish a robust cash management system, effectively control commitments, and initiate a medium-term budgeting framework for ministries.[11]

- **Strengthening the legal and institutional framework for public debt guarantees.** Guarantees have been used to secure better borrowing terms by statutory bodies and

[11] Weaknesses in effectively monitoring the stock of domestic arrears was brought to light by a recent incident where the government only recently acknowledged a claim for about EC$2 million. The work done by a contractor had apparently not been up to standards, and the government had failed to record the liability on its books until the work was completed recently.

are often requested by lenders. However, current procedures for guaranteeing debt are unsystematic, delinked from the government's other economic objectives, and offer few safeguards on the financial soundness of the underlying borrowing. The ministry of finance, with staff assistance, is working to strengthen this framework. The framework will involve ascertaining the financial soundness of the borrower and the borrowing plan, consistency with medium-term debt sustainability, transparency and parliamentary oversight in granting the guarantee, and monitoring the financial condition of the borrower for the duration of the guarantee.

Debt restructuring

28. **Staff called for a redoubling of efforts to complete the debt restructuring process, which has taken an unusually long time**. More than a year after the exchange offer formally closed in June 2004, the issuance of new bonds to all participating creditors has yet to be completed. The legislative changes that would allow these bonds to be traded on the Eastern Caribbean Stock Exchange (ECSE) also has yet to be passed by Parliament. The authorities attributed the delay to technical problems, limited domestic expertise, and difficulties in soliciting responses from nonparticipating (and some participating creditors). They committed to: (i) complete the issuance of the new bonds to all participating creditors shortly; and (ii) present legislative amendments at the next parliamentary sitting (expected in November) to allow ECSE trading of the bonds (MEP ¶7). The authorities reiterated their commitment to good-faith efforts to reach a collaborative settlement with the remaining creditors, and emphasized that they are treating outstanding principal amounts as if they had been restructured and are continuing to make deposits into an escrow account as payments fall due. They also noted that in late August they finally received communication from one of the three remaining large nonparticipating creditors and are hopeful of making further progress in the coming weeks. Staff cautioned that while payments into the escrow account underscored the authorities' positive approach to creditors, it did not preclude the risk of legal action by creditors as long as arrears are being incurred.

D. Addressing Vulnerabilities

29. **Discussions on policies to reduce vulnerabilities focused on strengthening the financial system and mitigating the costs of natural disasters.**

30. **Notwithstanding some banking system improvements, staff emphasized the need to monitor closely the recovery in credit growth and the quality of new lending**. The banking system was largely unaffected by the debt restructuring process, and appears broadly sound (Table 8). At end-June 2005, the capital adequacy ratios of locally incorporated banks was some 19 percent of risk-weighted assets, and the banking system's liquidity and profitability has been on the increase. But there remain concerns about banks ability to assess credit risk effectively, as nonperforming loans, while declining, are some 21 percent of total loans. Much of the recent credit expansion has occurred in the "personal loans" and "trade" categories, and staff queried the extent to which the former had been for business purposes,

and whether this reflected regulatory asymmetries for business versus personal loans. The authorities noted that some personal loans may well be used for business purposes, but thought that this likely reflected banks requests for personal collateral. Staff stressed the need for closer scrutiny on the quality of new lending, and urged the authorities to pass without delay the revised Banking Act, which would put in place some of the recommendations of the 2004 ECCU regional FSAP.

31. **The mission also called for steps to address vulnerabilities in the nonbank financial sector, particularly the credit unions**. Poor reporting practices and weak regulatory oversight have allowed credit union balance sheets to weaken over time, and the authorities have only started to address this problem in recent months. An onsite inspection of the Roseau Cooperative Credit Union (RCCU)—the largest credit union—undertaken in May, raised concerns about the level of nonperforming assets, account handling practices and the quality of the audit process. The recently established Financial Services Unit (FSU) is working with the RCCU to address the identified shortcomings, and is shortly also expected to carry out targeted inspections of the remaining 15 credit unions (MEP ¶10). Additionally, legislation is required to provide legal authority for the FSU to directly supervise the nonbank financial sector, including credit unions, money transfer institutions, and the AID Bank.

32. **Dominica's high vulnerability to natural disasters and recent experiences in the region underscore the need for better disaster-preparedness.** The November 2004 earthquake and mudslides had a large economic cost—estimated at around 7 percent of GDP—including through the fiscal accounts. The impact of future natural disasters could be reduced through better construction standards for roads and buildings, and greater risk mitigation could also be encouraged. However, improved building codes have not yet been legislated and not all government buildings and structures are insured. Staff also noted that the government might want to consider targeting a stronger primary balance, with a view to putting aside funds to cover the cost of any future natural disasters. The authorities saw merit in this proposal, but felt that additional fiscal adjustment at this time would be problematic. Instead, they are looking to participate in initiatives for regional risk pooling of catastrophe insurance.

V. Program Modalities

33. **Consistent with the increased focus on reinvigorating growth, the authorities program for 2005/06 has a stronger emphasis on structural reforms**. Two measures envisaged as prior actions for the completion of the fifth review have already been implemented: parliamentary approval of VAT legislation and Cabinet approval of a plan to rationalize the wage bill and ensure its consistency with the budgetary envelope. Reflecting implementation delays, two other structural benchmarks initially envisaged for end-September are now only expected to be completed by end-December (MEP Table 2). In the attached LOI and MEP, the authorities also:

- establish quantitative performance criteria for the end-December 2005 and end-June 2006 test dates, and indicative targets for end-September 2005 and March 2006;
- outline their structural reform agenda for the remainder of 2005 and the first few months of 2006 (Table 9); and
- request a waiver for the nonobservance of the continuous performance criteria on external payments arrears.

34. **The authorities also request the extension of repurchase expectations arising in the period from December 22, 2005 to December 22, 2006** (LOI ¶4). The original Stand-By Arrangement projected a balance of payments (BOP) deficit of 2.1 percent of GDP and a current account deficit of 12.9 percent of GDP for 2005. Current projections show larger deficits of approximately 3.1 percent for the overall balance of the BOP and 19.2 percent (17 percent on a cash basis) for the current account. In light of this and the fragile nature of the external accounts, staff supports this request. The extension would move the repurchase expectations totaling SDR 1,268,444 to an obligation basis, with each amount falling due exactly one year after the expectation date (Table 10).

VI. Other Issues

35. **Dominica's statistical databases remains weak, and substantial improvements are needed to ensure effective surveillance**. Dominica participates in the General Data Dissemination System (GDDS) and their metadata highlights some of the weaknesses and proposals for improvements within that framework. The mission recommended that priority be given to improving the quality and timeliness of debt data and more frequent surveys of living conditions.

36. **The authorities expressed grave concern about the implications of the planned erosion of banana preferences, and the consequent adverse effects on the economy**. They reiterated their commitment to regional integration through the OECS and CARICOM, and their intent to continue using CARICOM's regional negotiating machinery to negotiate more successfully in international fora. Government officials also indicated a revision of the tariff regime is underway to ensure the country's compliance with CARICOM's harmonized tariff schedule. In addition, the revision will remove import licensing requirements still in place.

37. **There is a dearth of data on labor market indicators**. The last labor force survey was carried out in 1999 (although a new one is underway), and there is little information on incomes. The current labor code is largely outdated, with minimum wage levels well below prevailing levels. Other broader policy-induced distortions are harder to discern.

VII. PRSP STATUS REPORT

38. **Preparation of the *Growth and Social Protection Strategy* (GSPS) is nearing completion**. In the attached preparation status report, the authorities note that a draft of GSPS was circulated for comment at a donors' conference held in Roseau in June. A revised draft reflecting these comments is currently being prepared and, after a final round of public consultations, the document is expected to be presented to Cabinet for adoption later this year. Staff called on the authorities to finalize the GSPS as soon as possible, including to help guide new projects under the PSIP. The authorities were confident that the sectoral strategies currently being developed as well as the FY 2005/06 PSIP are consistent with the GSPS.

VIII. STAFF APPRAISAL

39. **Dominica has made commendable progress under the PRGF-supported program**. The remarkable turnaround in the economy's fortunes to a large extent reflects the strong policies pursued by the authorities. With the confidence these policies have engendered, economic growth has resumed, financial intermediation has recovered, and tax revenues have been buoyant. The latter allowed the program's medium-term primary surplus objective to be realized sooner than expected.

40. **Staff also welcomes the stronger foundation that is being laid for public finances**. The adoption of VAT and excise tax legislation in early September should allow the introduction of VAT in March 2006. This will serve to widen the tax base and improve its structure and efficiency. The government's recent decision to publish Cabinet decisions on tax concessions is also a very important step toward improving the transparency of public finances. Provided amendments to the FAA include firm guidelines on targeting a primary fiscal surplus consistent with reducing the public debt stock to a prudent level, the scope for repeating the mistakes that caused debt to explode in the 1990s will have been minimized.

41. **But much remains to be done to sustain the current growth momentum**. Public debt, while trending downward, remains very high. Further, a number of threats to public finance have yet to be addressed, including from the large projected deficit of the social security system. The manner in which these issues are addressed will have a bearing on the durability of the economic recovery and sustainability of public finances. Moreover, these issues have to be addressed against the ever present specter of exogenous shocks, including from natural disasters. Key aspects of the Article IV consultation accordingly focused on policies to remove the impediments to growth and address the remaining threats to public finances.

42. **Removing bottlenecks that are impeding higher private investment has to become a central plank of the government's growth agenda**. Mindful of the limited implementation capacity, staff believes that the following reforms should be given priority. First, the Electricity Supply Act should be amended at the earliest opportunity to allow new

entrants into the market. Second, the enabling environment for private sector investment needs to be enhanced, including by rationalizing the operations of the three investment promotion agencies with a view to creating a one-stop investment promotion center. Third, the government should at the earliest opportunity adopt a program to modernize and ensure comprehensive coverage of land registration. In the long haul, such reforms will do more to stimulate private sector led growth than seeking to attract investment through tax incentives. In this context, the recent rise in the number of discretionary tax incentives is very disappointing, and the use of such incentives should be sharply curtailed going forward.

43. **Fiscal policy needs to remain geared towards further debt reduction**. Staff welcomes the 2005/06 budget which targets a primary surplus that appropriately balances further debt reduction with the need to reinstate the 5 percent cut in public wages introduced in 2003/04. Looking ahead, it will be important for the government to continue targeting a primary surplus of at least 3 percent of GDP to ensure a reduction in the debt stock to more manageable levels. Aiming to reduce debt to 60 percent of GDP over the next decade would be highly desirable. The efficiency of government spending also needs to be improved by further streamlining of public sector employment and limiting the PSIP to well-targeted projects with high returns. Staff strongly welcomes the government's objective of a smaller, more efficient and better paid public service. But to be consistent with further medium-term reductions in the wage bill, the structure and functions of ministries and departments need to be rationalized aggressively.

44. **The threat of the large unfunded social security liabilities jeopardizing debt sustainability needs to be addressed decisively and promptly**. The time when DSS will start to incur deficits is not far off. The sooner reforms are put in place, the more gradual and less abrupt these reforms will be. Consequently, staff urges the authorities to expedite the review and implementation of the reform options for addressing the looming social security system deficits. Given the country's vulnerability to natural disasters, international diversification of DSS's portfolio should be initiated at the earliest opportunity.

45. **With the renewed political mandate, the government has an unparalleled window of opportunity to advance reforms**. Reforms of the last few years have addressed the adverse effects on output growth stemming from the government's large fiscal deficits and arrears. The government should move quickly to remove the remaining impediments to higher economic growth and reduce the threats to public finance. Vulnerabilities in the financial sector also need to be addressed quickly by strengthening regulatory oversight of nonbank institutions.

46. **The current monetary and exchange rate arrangement has served Dominica well**. Staff fully concurs with the authorities' assessment that the framework needs to remain the bulwark around which economic policies should be based. The regional currency board arrangement has provided the country with a remarkable period of exchange rate and price stability even in the presence of frequent and large adverse shocks. The depreciation of the

U.S. dollar in recent years has helped move the real exchange rate well within a manageable range.

47. **Dominica continues to make progress in the provision of core statistics to the Fund**. However, data deficiencies continue to hamper surveillance purposes. Staff encourages the authorities to improve data quality, in particular on national accounts and government finances.

48. **Staff recommends completion of the financing assurances review**. This is warranted in light of the authorities' good faith efforts in seeking collaborative settlements with the remaining private nonparticipating creditor and best efforts to reach agreement with the remaining bilateral creditors, willingness to continue depositing payments into an escrow account, as well as the strong reform agenda it is pursuing. While risks to Fund resources will remain until the debt restructuring process is completed and all external arrears are eliminated, the critical role of Fund support for the success of the authorities' program is further justification for the completion of the financing assurances review.

49. **Finally, staff supports**:

- **Granting the requested waiver** for the nonobservance of the continuous performance criterion on the nonaccumulation of external payments arrears in light of the minor and temporary nature of the deviation.

- **The authorities' request to extend the repurchase expectations**. Despite the recent improvement in economic conditions, Dominica's external position remains weak. Repayment on an expectation basis of the purchases made under the 2002 SBA would impose undue hardship and heighten risks to the current PRGF arrangement.

- **The conclusion of the fifth review** as program implementation has been solid. All-but-one performance criteria under the arrangement have been observed, most by large margins. While significant risks remain, the authorities' commitment to implementing the policies envisaged under the program and thus address these should help maintain a satisfactory performance.

50. It is recommended that the next Article IV consultation with Dominica be held under the 24-month cycle, in accordance with the provisions of Decision No. 12794-(02/76) of July 15, 2002.

Table 1. Dominica: Selected Economic and Social Indicators, 2001–2006

	2001	2002	2003	2004	Prog. 1/ 2005	Proj. 2005	Prog. 2006
(Annual percent change, unless otherwise specified)							
Output and prices							
Real GDP (factor cost)	-4.2	-4.7	0.0	3.5	2.5	3.1	3.0
GDP deflator (factor cost)	1.2	-0.4	1.7	1.2	1.5	1.5	1.5
Nominal GDP (at factor cost)	-3.0	-5.1	1.7	4.7	4.1	4.5	4.5
Nominal GDP at market prices	-2.7	-3.7	2.4	5.0	3.9	4.3	4.4
Consumer prices (end of period)	1.1	0.4	2.9	0.8	1.5	1.5	1.5
Money and credit							
Net foreign assets of the banking system 2/	6.6	19.3	17.3	8.1	4.1	4.1	5.5
Net domestic assets of the banking system 2/	0.9	-10.8	-16.4	-2.1	1.4	1.9	0.6
Of which							
Net credit to the nonfinancial public sector 2/	5.6	-5.4	-4.3	-5.1	0.1	0.2	-1.7
Credit to the private sector 2/	-3.1	-1.3	-2.3	4.3	4.8	5.1	4.1
Liabilities to the private sector (M2)	7.4	8.5	1.0	5.9	5.5	6.0	6.1
Balance of payments							
Merchandise exports, f.o.b.	-18.9	-1.8	-6.0	3.0	6.9	5.2	5.0
Merchandise imports, f.o.b.	-11.3	-11.5	9.3	13.5	3.7	8.6	4.0
Real effective exchange rate							
(end-of-period; depreciation -) 3/	3.7	-6.3	-6.7	-7.0	…	-3.5	…
(In millions of U.S. dollars)							
Merchandise exports, f.o.b.	44.4	43.6	41.0	42.2	45.2	44.5	46.7
Merchandise imports, f.o.b.	115.7	102.4	111.8	126.9	131.6	137.8	143.2
Current account balance	-48.9	-34.7	-33.6	-46.7	-42.4	-54.3	-51.8
Capital account balance 4/	50.3	46.9	35.0	20.9	32.7	45.4	43.6
Overall balance	1.5	12.1	1.4	-25.7	-9.7	-8.8	-8.2
(In percent of GDP, unless otherwise specified)							
Central government 5/							
Savings	-3.0	-0.6	8.7	7.6	8.1	7.4	8.2
Of which							
Primary	2.4	5.1	14.6	13.8	14.0	13.1	13.1
Grants	1.7	4.5	8.8	5.9	6.2	8.1	8.1
Capital expenditure and net lending	5.7	5.1	10.1	8.5	11.0	10.1	10.1
Primary balance	-2.1	-1.6	5.6	4.4	3.0	3.0	3.0
Overall balance	-8.6	-5.4	-1.3	-0.6	-2.5	-2.5	-1.7
Nonfinancial public sector debt (gross)							
Total	93.7	127.2	130.6	116.7	...	109.1	103.9
External	67.5	79.9	84.4	81.2	...	81.1	77.6
Domestic	26.2	47.3	46.2	35.5	...	28.0	26.3
External sector							
Current account balance	-18.7	-13.8	-13.0	-17.2	-15.2	-19.2	-17.6
External public debt service 6/	10.9	11.8	19.5	20.8	11.2	15.9	13.1
Amortization	4.5	4.6	12.8	14.1	5.3	8.2	7.3
Interest	6.4	7.1	6.8	6.7	5.9	7.6	5.8
Memorandum items:							
Nominal GDP at market prices (EC$ millions)							
Calendar year	706.8	680.5	697.1	731.7	754.2	763.5	796.9
Net international reserves							
(U.S. dollars millions; end-of-period) 7/	30.4	43.6	44.0	33.6	34.0	38.9	41.0

Sources: Dominican authorities; Eastern Caribbean Central Bank (ECCB); and Fund staff estimates and projections.

1/ IMF Country Report No. 05/117.
2/ Change relative to the stock of M2 at the beginning of the period. From 2003, transactions with the IMF are included as transactions of the monetary authorities.
3/ Figure for 2005 is for the 12-month period to June 2005.
4/ Including errors and omissions.
5/ These data are presented on a fiscal year (July–June) basis. Figures shown for a given calendar year relate to the fiscal year beginning on July 1 of that year.
6/ On a due basis (i.e., before restructuring). In percent of exports of goods and nonfactor services.
7/ Imputed reserves at the ECCB until 2001. From 2002, transactions with the IMF are included as transactions of the monetary authorities.

Table 2. Dominica: Summary Accounts of the Central Government, 2000/01–2005/06 1/

	2000/01	2001/02	2002/03	2003/04	2004/05 3/ Prog. 2/	2004/05 3/ Prov.	2005/06 Prog. 2/	2005/06 Rev. Prog.
(In millions of Eastern Caribbean dollars)								
Total revenue and grants	**271.5**	**209.7**	**224.1**	**285.9**	**291.3**	**292.0**	**287.0**	**294.2**
Current revenue	200.5	197.1	191.9	221.8	229.2	245.7	237.2	229.3
Capital revenue	3.0	0.9	1.3	1.0	2.5	2.0	2.6	1.5
Grants	68.0	11.8	30.9	63.2	59.6	44.3	47.3	63.4
Total expenditure	**350.3**	**269.3**	**261.3**	**295.2**	**317.5**	**296.3**	**306.4**	**313.5**
Current expenditure	230.1	229.7	226.6	223.1	226.7	232.9	222.2	234.8
Wages and salaries 4/	116.2	116.5	116.1	104.2	102.7	102.0	99.7	106.5
Interest	36.0	36.9	37.6	41.7	43.8	43.9	42.4	43.0
Others	77.9	76.3	72.8	77.2	80.1	87.0	80.1	85.3
Capital expenditure and net lending	120.2	39.6	34.7	72.1	90.9	63.5	84.2	78.7
Overall balance	**-78.8**	**-59.5**	**-37.2**	**-9.3**	**-26.3**	**-4.3**	**-19.3**	**-19.3**
Statistical discrepancy 5/	18.7	8.2	-11.5	7.7	-2.7	-7.0	0.0	0.0
Financing	**60.1**	**51.3**	**48.7**	**1.6**	**29.0**	**11.3**	**19.3**	**19.3**
Net foreign financing	42.7	25.6	44.9	47.3	16.9	19.6	12.5	22.3
Disbursements	...	31.9	47.7	78.4	20.9	24.5	11.5	11.8
Amortization	...	6.3	6.5	37.2	43.2	43.2	20.2	20.4
Other including rescheduling	...	0.0	3.8	6.1	39.2	38.3	21.2	30.8
Net domestic financing	17.4	25.7	3.8	-45.7	12.1	-8.3	6.8	-3.0
Bank	11.2	16.3	-6.9	-41.4	-0.2	-15.3	-2.9	-13.6
Nonbank	6.2	9.5	10.7	-8.8	1.6	-3.2	0.0	0.0
Other including rescheduling	0.0	0.0	0.0	4.6	10.7	10.2	9.7	10.6
(In percent of GDP)								
Total revenue and grants	**37.6**	**30.2**	**32.7**	**40.0**	**39.4**	**39.1**	**37.4**	**37.7**
Current revenue	27.8	28.4	28.0	31.0	31.0	32.9	30.9	29.4
Capital revenue	0.4	0.1	0.2	0.1	0.3	0.3	0.3	0.2
Grants	9.4	1.7	4.5	8.8	8.1	5.9	6.2	8.1
Total expenditure	**48.5**	**38.8**	**38.2**	**41.3**	**42.9**	**39.6**	**39.9**	**40.2**
Current expenditure	31.9	33.1	33.1	31.2	30.6	31.1	28.9	30.1
Wages and salaries 4/	16.1	16.8	17.0	14.6	13.9	13.6	13.0	13.7
Interest	5.0	5.3	5.5	5.8	5.9	5.9	5.5	5.5
Others	10.8	11.0	10.6	10.8	10.8	11.6	10.4	10.9
Capital expenditure and net lending	16.6	5.7	5.1	10.1	12.3	8.5	11.0	10.1
Overall balance	**-10.9**	**-8.6**	**-5.4**	**-1.3**	**-3.5**	**-0.6**	**-2.5**	**-2.5**
Statistical discrepancy 5/	2.6	1.2	-1.7	1.1	-0.4	-0.9	0.0	0.0
Financing	**8.3**	**7.4**	**7.1**	**0.2**	**3.9**	**1.5**	**2.5**	**2.5**
Net foreign financing	5.9	3.7	6.6	6.6	2.3	2.6	1.6	2.9
Disbursements	...	4.6	7.0	11.0	2.8	3.3	1.5	1.5
Amortization	...	0.9	1.0	5.2	5.8	5.8	2.6	2.6
Other including rescheduling	...	0.0	0.6	0.9	5.3	5.1	2.8	3.9
Net domestic financing	2.4	3.7	0.6	-6.4	1.6	-1.1	0.9	-0.4
Bank	1.5	2.3	-1.0	-5.8	0.0	-2.0	-0.4	-1.7
Nonbank	0.9	1.4	1.6	-1.2	0.2	-0.4	0.0	0.0
Other including rescheduling	0.0	0.0	0.0	0.6	1.4	1.4	1.3	1.4
Memorandum items:								
Capital expenditure less total grants								
In EC$ million	42.9	30.2	4.0	11.8	34.7	22.8	39.5	17.9
In percent of GDP	5.9	4.3	0.6	1.7	4.7	3.0	5.1	2.3
Savings (incl. grants)	5.3	-3.0	-0.6	8.7	8.4	7.6	8.1	7.4
Primary savings (before grants)	1.3	0.7	0.6	5.8	6.6	7.9	7.8	5.0
Primary balance (incl. grants) 6/	-3.3	-2.1	-1.6	5.6	2.0	4.4	3.0	3.0
Nominal GDP at market prices (EC$ millions)	722.4	693.7	684.8	714.4	740.0	747.6	767.5	780.2

Sources: Ministry of Finance; and Fund staff estimates and projections.

1/ Fiscal years beginning July 1.
2/ IMF Country Report No. 05/117.
3/ On a commitment basis.
4/ 2005/06 includes a reclassification of EC$2.3 million (0.3 percent of GDP) to other expenditure, reflecting a transfer of teachers from the government payroll to that of the State College.
5/ Difference between identified financing below-the-line and overall balance above-the-line. Projected discrepancy for FY 2004/2005 equals realized discrepancy through end-May 2005.
6/ Computed using overall deficit measured from below-the-line.

Table 3. Dominica: Balance of Payments 2002–2010

	2002	2003	Prel. 2004	Prog. 1/ 2005	Proj. 2005	Prog. 2006	Proj. 2007	Proj. 2008	Proj. 2009	Proj. 2010
	(In millions of U.S. dollars)									
Current account balance	**-34.7**	**-33.6**	**-46.7**	**-42.4**	**-54.3**	**-51.8**	**-50.5**	**-48.9**	**-47.6**	**-45.9**
Trade balance	-58.7	-70.8	-84.6	-86.4	-93.3	-96.5	-98.4	-100.2	-102.4	-104.6
Exports (f.o.b.) 2/	43.6	41.0	42.2	45.2	44.5	46.7	49.1	51.5	54.1	56.8
Of which										
Bananas	8.1	5.9	7.2	...	7.2	7.5	7.8	8.2	8.5	8.9
Imports (f.o.b.)	102.4	111.8	126.9	131.6	137.8	143.2	147.5	151.8	156.5	161.4
Services balance	26.0	32.8	40.0	47.8	45.1	47.3	50.1	53.1	56.2	59.3
Exports of services	79.7	77.3	86.3	107.2	95.5	99.6	104.0	108.5	113.3	118.3
Travel	45.7	52.3	60.1	68.7	65.6	68.5	71.5	74.6	77.9	81.3
Other	34.0	25.0	26.2	38.5	29.8	31.1	32.5	33.9	35.4	37.0
Imports of services	53.7	44.6	46.3	59.4	50.3	52.3	53.9	55.4	57.1	59.0
Net income	-18.4	-12.1	-21.8	-20.9	-22.0	-20.2	-20.6	-20.9	-21.4	-21.5
Interest payments (public sector)	-8.8	-8.0	-8.6	-9.0	-10.7	-8.4	-8.3	-8.1	-8.0	-7.5
Other income	-9.6	-4.1	-13.2	-11.9	-11.3	-11.8	-12.3	-12.9	-13.4	-14.0
Net current transfers	16.4	16.6	19.8	17.1	15.9	17.6	18.4	19.2	20.0	20.9
Private	12.6	12.4	18.4	16.9	17.0	17.7	18.5	19.3	20.1	21.0
Public	3.8	4.2	1.4	0.2	-1.1	-0.1	-0.1	-0.1	-0.1	-0.1
Capital and financial account	**32.1**	**22.4**	**23.0**	**32.7**	**45.4**	**43.6**	**50.4**	**47.5**	**43.8**	**52.1**
Capital account	20.5	18.8	26.8	22.6	19.2	26.7	28.1	29.3	30.6	32.0
Public capital transfers	17.7	15.9	23.8	19.6	16.3	23.7	25.0	26.1	27.3	28.4
Private capital transfers	2.8	2.9	3.0	3.0	2.8	3.0	3.1	3.2	3.4	3.5
Financial account	11.6	3.7	-3.8	10.1	26.3	16.9	22.3	18.2	13.2	20.1
Public sector	25.8	8.9	0.2	-0.3	-1.3	-6.2	-6.7	-6.9	-9.4	-4.8
Budgetary flows (net)	25.0	8.9	0.2	-0.3	-1.3	-6.2	-6.7	-6.9	-9.4	-4.8
Disbursements	30.7	24.0	18.3	7.8	10.2	4.4	4.6	4.8	5.0	5.3
Repayments	5.7	15.1	18.1	8.0	11.5	10.7	11.4	11.7	14.5	10.0
Nonbudgetary flows (net)	0.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Private sector	-14.1	-5.2	-4.0	10.3	27.6	23.1	29.1	25.1	22.6	24.9
Direct investment	11.4	19.8	18.1	21.1	21.1	21.7	22.4	23.0	23.7	24.4
Commercial banks	-24.1	-33.9	-26.9	-9.0	-3.6	-10.5	-6.3	-7.9	-5.0	-2.5
Other private flows	-1.5	8.8	4.8	-1.8	10.0	11.9	13.0	10.0	3.9	3.0
Errors and omissions	**14.7**	**12.5**	**-2.1**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Overall balance	**12.1**	**1.4**	**-25.7**	**-9.7**	**-8.8**	**-8.2**	**-0.1**	**-1.3**	**-3.8**	**6.2**
Overall financing	**-12.1**	**-1.4**	**25.7**	**9.7**	**8.8**	**8.2**	**0.1**	**1.3**	**3.8**	**-6.2**
Net international reserves	-12.1	-1.4	10.3	-0.4	-5.3	-2.1	-4.9	-3.2	-3.5	-3.9
Gross reserves (increase = -)	-15.1	-6.2	9.4	-3.5	-8.5	-3.9	-3.1	-2.6	-2.7	-2.9
IMF reserve liabilities (purchase = +)	3.0	4.8	0.9	3.1	3.2	1.8	-1.8	-0.6	-0.7	-1.1
Exceptional financing	0.0	0.0	15.4	10.1	14.1	10.4	5.0	4.5	7.2	-2.3
	(In percent of GDP)									
Memorandum items:										
Current account balance	-13.8	-13.0	-17.2	-15.2	-19.2	-17.6	-16.4	-15.2	-14.2	-13.1
Current account balance including net capital transfers	-5.6	-5.7	-7.3	-7.1	-12.4	-8.5	-7.3	-6.1	-5.0	-4.0
External public debt service (as a percent of exports of goods and nonfactor services)	11.8	19.5	20.8	11.2	15.9	13.1	12.8	12.4	13.4	10.0
Amortization	4.6	12.8	14.1	5.3	8.2	7.3	7.4	7.3	8.6	5.7
Interest	7.1	6.8	6.7	5.9	7.6	5.8	5.4	5.0	4.8	4.3

Sources: Dominican authorities; Eastern Caribbean Central Bank (ECCB); and Fund staff estimates and projections.

1/ IMF Country Report No. 05/117.
2/ Includes stores and bunkers.

Table 4. Dominica: Summary Accounts of the Banking System, 2002–2006

	2002	2003	2004	Prog. 1/ 2005	Proj. 2005	Proj. 2006
	I. Consolidated Banking System and Monetary Authorities					
	(In millions of Eastern Caribbean dollars, end of period)					
Net foreign assets	**193.8**	**289.0**	**333.7**	**357.7**	**357.5**	**391.6**
Net domestic assets	**355.4**	**265.5**	**253.6**	**261.7**	**264.8**	**268.8**
Net credit to the nonfinancial public sector	74.8	51.1	23.0	23.6	24.1	13.6
Of which						
Central government	64.2	55.9	45.6	46.6	50.7	37.4
Net credit to nonbank financial institutions	-46.6	-81.8	-75.9	-78.8	-79.1	-82.6
Credit to the private sector	433.2	420.6	444.7	472.9	474.7	500.2
Other items (net) 2/	-106.1	-124.5	-138.2	-155.9	-154.8	-162.5
Broad money 3/	**549.2**	**554.5**	**587.4**	**619.5**	**622.4**	**660.4**
	II. Operations of the Monetary Authorities					
Imputed net international reserves	**117.8**	**118.7**	**90.8**	**91.8**	**105.0**	**110.8**
Net domestic assets	**12.1**	**7.0**	**26.0**	**27.9**	**18.7**	**20.5**
Monetary base	**129.9**	**125.7**	**116.8**	**119.7**	**123.7**	**131.3**
Currency in circulation	35.5	34.2	37.6	38.9	39.0	40.7
Commercial bank reserves	94.4	91.5	79.2	80.8	84.7	90.6
	III. Commercial Banks					
Net foreign assets	**79.0**	**170.4**	**242.9**	**265.9**	**252.5**	**280.8**
Net claims on ECCB	**98.2**	**85.6**	**73.8**	**78.8**	**78.9**	**84.4**
Net domestic assets	**336.6**	**264.3**	**233.1**	**235.8**	**251.9**	**254.5**
Net credit to the nonfinancial public sector	53.4	26.3	-10.8	-16.0	-15.9	-29.0
Net credit to nonbank financial institutions	-46.6	-81.8	-75.9	-78.8	-79.1	-82.6
Credit to the private sector	433.2	420.6	444.7	472.9	474.7	500.2
Other (net)	-103.5	-100.7	-125.0	-142.2	-127.7	-134.1
Private sector deposits 3/	**513.7**	**520.3**	**549.8**	**580.6**	**583.4**	**619.7**
	IV. Consolidated Banking System					
	(Annual percentage change)					
Credit to the private sector	-1.4	-2.9	5.7	6.3	6.7	5.4
Private sector deposits	7.6	1.3	5.7	6.1	12.7	6.2
Broad money	8.5	1.0	5.9	5.5	6.0	6.1
	(Contributions to liquidity growth) 4/					
Net foreign assets	**19.3**	**17.3**	**8.1**	**4.1**	**4.1**	**5.5**
Net domestic assets	**-10.8**	**-16.4**	**-2.1**	**1.4**	**1.9**	**0.6**
Net credit to the nonfinancial public sector	-5.4	-4.3	-5.1	0.1	0.2	-1.7
Credit to the private sector	-1.3	-2.3	4.3	4.8	5.1	4.1
Memorandum items:						
Interest rates 5/						
Deposits (three-month time—maximum rate)	6.0	6.0	3.0	…	…	…
Lending: Minimum rate	8.5	8.0	7.5	…	…	…
Maximum rate	20.8	18.2	18.2	…	…	…

Sources: Eastern Caribbean Central Bank (ECCB); and Fund staff estimates and projections.

1/ Program figures are as shown in IMF Country Report No. 05/117. From 2002, transactions with the IMF are included as transactions with the monetary authorities.
2/ Includes interbank float.
3/ Including foreign currency deposits.
4/ Change relative to broad money at the beginning of the period.
5/ Commercial banks; end-of-period rates, percent per annum.

Table 5. Dominica: Quantitative Performance Criteria (PC) and Indicative Targets (IT)

	Program PC	Adjusted PC	Actual	Margin (+)/ Excess (-)	Program PC	Adjusted PC	Actual	Margin (+)/ Excess (-)	Program IT	Adjusted IT	Actual	Margin (+)/ Excess (-)	Program PC	Adjusted PC	Prov. Actual	Margin (+ Excess (-)
	Sept. 30, 2004 1/				Dec. 31, 2004 1/				Mar. 31, 2005 1/				June. 30, 2005 1/			
I. Performance Criteria																
(In millions of Eastern Caribbean dollars)																
Central government primary balance	-3.0	-3.0	0.2	3.2	3.0	3.0	14.7	11.7	11.0	11.0	23.8	12.8	14.4	8.5	32.6	24.1
Central government wage bill	27.0	27.0	25.3	1.7	54.0	54.0	51.5	2.5	78.5	78.5	77.4	1.1	104.2	104.2	102.0	2.2
Banking system net credit to central government	3.0	6.7	4.0	2.6	3.0	6.0	-2.0	8.0	0.0	3.7	-6.7	10.5	0.0	4.7	-15.3	20.0
Net changes in central government arrears to private domestic parties	15.0	15.0	3.2	11.8	15.0	15.0	4.1	10.9	15.0	15.0	4.5	10.5	15.0	15.0	3.8	11.2
(In millions of U.S. dollars)																
Disbursement of central government or central government guaranteed external nonconcessional debt with maturity of at least one year	4.0	4.0	2.9	1.1	6.0	6.0	3.4	2.6	8.0	8.0	4.4	3.6	10.0	10.0	5.3	4.7
Net changes in the outstanding stock of contracted or guaranteed short-term external debt of the central government (with maturity of less than one year) 2/	0.0	0.0	Met	...	0.0	0.0	Met	...	0.0	0.0	Met	...	0.0	0.0	Met	...
Central government and central government guaranteed external payments arrears 2/ 3/	0.0	0.0	Not met	...	0.0	0.0	Not met	...	0.0	0.0	Met	...	0.0	0.0	Not met	...
II. Indicative Targets																
(In millions of Eastern Caribbean dollars)																
Central government overall balance	-16.7	-16.7	-13.3	3.4	-19.6	-19.6	-7.4	12.1	-25.6	-25.6	-11.9	13.7	-32.0	-37.9	-11.3	26.6
Central government revenues	48.7	48.7	55.4	6.7	103.6	103.6	116.5	12.9	160.3	160.3	175.4	15.1	210.6	210.6	245.1	34.6
Central government primary savings	4.1	4.1	12.3	8.2	15.2	15.2	27.3	12.1	29.6	29.6	42.2	12.6	35.4	35.4	58.7	23.3

Sources: Dominican authorities; Eastern Caribbean Central Bank (ECCB); and Fund staff estimates and projections.

1/ Cumulative amounts from June 30, 2004. All variables and adjustors that apply are defined in the Technical Memorandum of Understanding.
2/ These performance criteria will be monitored on a continuous basis.
3/ External arrears that were known at the time of the Executive Board discussions on August 4, 2004 and on March 7, 2005, were waived.

Table 6. Dominica: Structural Benchmarks and Status of Structural Reforms

	Category	Target Date or Completion Date	Status
Finalize proposals for amending the Finance Administration Act, to implement a Fiscal Responsibility Law.	Benchmark	July 2005	Completed
Approval of the 2005/06 budget, with a primary balance target consistent with the PRGF program.	Benchmark	August 2005	Completed
Financial sector reforms			
On-site inspection of Roseau Credit Union and follow-up on findings/remedial measures.	Benchmark	June 2005	Completed
Establish legislative basis for the FSU to supervise insurance companies, and regulate all NBFIs and AID Bank.	Benchmark	End-September 2005	Ongoing
Other reforms			
Cabinet approval of action plans for DEXIA and NDC, addressing their reorganization and cost effectiveness.	Benchmark	End-September 2005	Pending

Sources: Dominican authorities; and IMF Country Report No. 05/117.

Table 7. Dominica: Medium-Term Macroeconomic Framework, 2000–2010

	2000	2001	2002	2003	Est. 2004	Prog. 1/ 2005	Proj. 2005	Proj. 2006	Proj. 2007	Proj. 2008	Proj. 2009	Proj. 2010
	(Annual percent change)											
National income and prices												
GDP at constant (1990) prices	1.4	-4.2	-4.7	0.0	3.5	2.5	3.1	3.0	3.0	3.0	3.0	3.0
Implicit GDP deflator (factor cost)	0.6	1.2	-0.4	1.7	1.2	1.5	1.5	1.5	1.5	1.5	1.5	1.5
	(In percent of GDP, unless otherwise specified)											
Savings and investment												
Gross domestic investment	**27.7**	**25.4**	**20.9**	**25.4**	**28.9**	**22.1**	**24.9**	**26.7**	**27.7**	**27.7**	**27.7**	**27.7**
Public	18.6	15.0	7.5	9.4	11.8	13.1	9.9	10.7	10.7	10.7	10.7	10.7
Of which												
Central government	15.3	10.7	5.6	7.8	9.7	12.1	9.7	10.4	10.4	10.4	10.4	10.4
Rest of public sector	3.2	4.3	1.9	1.6	2.0	1.0	0.3	0.3	0.3	0.3	0.3	0.3
Private	9.1	10.3	13.4	16.0	17.1	9.0	15.0	16.0	17.0	17.0	17.0	17.0
Gross national saving 2/	**12.0**	**13.6**	**15.3**	**19.7**	**21.6**	**15.0**	**12.5**	**18.2**	**20.4**	**21.6**	**22.6**	**23.7**
Public	3.7	3.6	0.0	5.9	10.8	10.0	8.4	8.6	9.0	9.2	9.5	9.6
Of which												
Central government	1.8	1.0	-1.4	4.4	8.8	9.0	8.2	8.3	8.8	9.0	9.2	9.4
Rest of public sector	1.9	2.6	1.4	1.5	2.0	1.0	0.3	0.3	0.3	0.3	0.3	0.3
Private	8.3	10.0	15.3	13.8	10.8	5.0	4.1	9.6	11.4	12.3	13.2	14.1
Savings investment balance	**-15.7**	**-11.8**	**-5.6**	**-5.7**	**-7.3**	**-7.1**	**-12.4**	**-8.5**	**-7.3**	**-6.1**	**-5.0**	**-4.0**
Public savings investment	-14.8	-11.5	-7.5	-3.5	-1.0	-3.0	-1.5	-2.1	-1.6	-1.4	-1.2	-1.0
Private savings investment	-0.9	-0.3	1.8	-2.3	-6.3	-4.0	-10.9	-6.4	-5.6	-4.7	-3.8	-2.9
Memorandum items:												
Nonfinancial public sector debt	86.2	93.7	127.2	130.6	116.7	...	109.1	103.9	99.5	95.3	91.1	87.1
External	56.4	67.5	79.9	84.4	81.2	...	81.1	77.6	72.9	68.5	64.2	58.7
Domestic	29.8	26.2	47.3	46.2	35.5	...	28.0	26.3	26.6	26.7	26.9	28.4

Sources: Dominican authorities; Eastern Caribbean Central Bank (ECCB); and Fund staff estimates and projections.

1/ IMF Country Report No. 05/117.
2/ Calculated using the external current account including net external capital transfers.

Table 8. Dominica: Financial and External Vulnerability Indicators, 2000–2005

(In percent of GDP, unless otherwise indicated)

	2000	2001	2002	2003	2004	Proj. 2005
Financial indicators						
Broad money (percent change, 12-month basis)	0.6	7.4	8.5	1.0	5.9	6.0
Private sector credit (percent change, 12-month basis)	8.2	-3.2	-1.4	-2.9	5.7	6.7
Unsatisfactory assets/total loans 1/	17.4	22.6	19.2	21.7	22.5	20.5
Provision for loan losses/total loans 1/	7.0	6.8	7.0	7.6	7.3	6.0
General and specific provisions for loan losses/unsatisfactory assets 1/	40.0	30.2	36.7	34.8	32.2	29.1
Specific provisions for loan losses/unsatisfactory assets 1/	33.3	26.2	32.6	30.1	...	...
Total capital/risk weighted assets (locally incorporated banks) 1/	30.8	35.4	34.1	28.5	23.0	18.7
Tier 1 capital/risk weighted assets (locally incorporated banks) 2/	27.4	34.1	32.9	28.1	23.0	18.7
Three-month treasury bill rate (end of period)	6.4	6.4	6.4	6.4	6.4	...
Three-month treasury bill rate (real) 2/	5.3	5.3	6.0	3.5	4.9	...
External indicators						
Exports of goods and services (percent change, 12-month basis in U.S. dollars)	-7.9	-16.9	2.7	-4.0	8.7	8.8
Imports of goods and services (percent change, 12-month basis in U.S. dollars)	1.4	-9.5	-5.8	0.2	10.8	8.6
Current account balance	-19.7	-18.7	-13.8	-13.0	-17.2	-19.2
Capital and financial account balance 3/	18.8	19.2	18.6	13.5	7.7	16.1
Net official reserves (in millions of U.S. dollars, end of period) 4/	29.0	30.4	43.6	44.0	33.6	38.9
Net reserves to broad money (percent, end of period) 3/	16.6	16.2	21.4	21.4	15.5	16.9
Public sector external debt	56.4	67.5	79.9	84.4	81.2	81.1
External debt (end of period) to exports of goods and services (percent) 5/	105.1	147.1	163.4	184.2	171.1	163.9
External interest payments to exports of goods and services (percent) 5/	4.3	6.4	7.1	6.8	6.7	7.6
External amortization payments to exports of goods and services (percent) 5/	3.1	4.5	4.6	12.8	14.1	8.2
Exchange rate (per U.S. dollar, end of period)	2.7	2.7	2.7	2.7	2.7	2.7
REER appreciation (end of period; depreciation -)	4.8	3.7	-6.3	-6.7	-7.0	-3.5

Sources: Eastern Caribbean Central Bank (ECCB); and Fund staff estimates and projections.

1/ Figure for 2005 is the provisional data for June 2005.
2/ Treasury bill rate adjusted by end-of-period inflation.
3/ Includes errors and omissions.
4/ Imputed reserves at the ECCB until 2001. From 2002, transactions with the IMF are included as transactions of the monetary authorities.
5/ Refers to public sector debt.

Table 9. Dominica: Schedule of Disbursements Under the PRGF Arrangement

	Disbursements (in millions)		As Percent	
	US$ 1/	SDR	of Quota	Conditions
2003	**3.419**	**2.358**	**28.8**	
December 29	3.419	2.358	28.8	Board approval of PRGF; and adoption of prior actions
2004	**0.893**	**0.616**	**7.5**	
March 31	0.447	0.308	3.8	First review under the PRGF; end-December 2003 performance criteria; and adoption of prior action.
August 10	0.447	0.308	3.8	Second review under the PRGF; and end-March 2004 performance criteria
2005	**3.468**	**2.392**	**29.2**	
March 22	1.785	1.231	15.0	Third and fourth reviews under the PRGF; end-June 2004, end-September 2004, and end-December 2004 performance criteria.
October 14	1.683	1.161	14.2	Fifth review under the PRGF; and end-June 2005 performance criteria.
2006	**3.367**	**2.322**	**28.3**	
March 15	1.683	1.161	14.2	Sixth review under the PRGF; and end-December 2005 performance criteria.
August 15	1.683	1.161	14.2	Seventh review under the PRGF; and end-June 2006 performance criteria.
Total	**11.148**	**7.688**	**93.8**	
Memorandum item:				
Quota (in millions)	11.890	8.200	100.0	

Source: Fund staff estimates and projections.

1/ For illustrative purposes only, SDR amounts have been converted into U.S. dollars at an US$/SDR exchange rate of 1.45.

Table 10. Dominica: Indicators of Capacity to Repay the Fund, 2003–2010

	2003	2004	Projections 2005	2006	2007	2008	2009	2010
(In millions of SDRs, unless otherwise specified)								
Obligations from existing drawings								
Repurchases:								
Expectation basis	0.00	0.00	0.29	2.29	0.38	0.00	0.50	0.50
Obligation basis	0.00	0.00	0.26	1.10	1.23	0.38	0.50	0.72
Charges/interest under expectations/obligations schedule for repurchases:								
Expectation basis	0.05	0.09	0.13	0.10	0.04	0.04	0.03	0.03
Obligation basis	0.05	0.09	0.13	0.13	0.08	0.05	0.04	0.03
Fund repurchases and charges (obligation basis) 1/								
In millions of SDRs	0.05	0.09	0.40	1.24	1.33	0.45	0.55	0.77
On existing credits	0.05	0.09	0.39	1.23	1.31	0.43	0.54	0.75
Of which								
Repurchases on an obligation basis	0.00	0.00	0.26	1.10	1.23	0.38	0.50	0.72
In millions of U.S. dollars	0.07	0.13	0.59	1.81	1.94	0.65	0.81	1.12
In percent of exports of goods and services	0.06	0.10	0.41	1.23	1.26	0.41	0.48	0.67
In percent of debt service 2/	0.30	0.50	2.59	8.74	9.04	3.20	3.49	6.02
In percent of quota	0.61	1.09	4.82	15.16	16.20	5.45	6.77	9.36
In percent of net international reserves 3/	0.16	0.39	1.72	4.80	4.70	1.50	1.76	2.44
Fund credit outstanding 1/								
In millions of SDRs	5.3	5.9	8.1	9.3	8.1	7.7	7.2	6.5
In millions of U.S. dollars	7.5	8.8	12.0	13.5	11.8	11.2	10.5	9.4
In percent of exports of goods and services	6.3	6.8	8.4	9.2	7.7	7.0	6.2	5.6
In percent of debt service 2/	32.3	33.0	53.0	65.4	54.9	55.1	45.2	50.7
In percent of quota	65.0	72.5	98.5	113.4	98.4	93.7	87.6	78.8
In percent of net international reserves 3/	17.0	26.2	35.1	35.9	28.6	25.7	22.8	20.5
Memorandum items:								
Exports of goods and services (millions of U.S. dollars)	118.3	128.6	143.0	146.9	153.6	160.6	167.8	167.8
Debt service (millions of U.S. dollars) 2/	23.1	26.7	22.6	20.7	21.4	20.4	23.2	18.6

Sources: Dominican authorities; Eastern Caribbean Central Bank (ECCB); and Fund staff estimates and projections.

1/ Including assumed future disbursements under the PRGF, and assuming all repurchases on an obligation basis.

2/ Including IMF repurchases in total debt service.

3/ Net international reserves of the monetary authorities; net imputed reserves of the ECCB and transactions with the Fund.

Table 11. Dominica: Millennium Development Goals 1/ 2/

	1990	1994	1997	2000	2003
Goal 1: Eradicate extreme poverty and hunger					
Percentage share of income or consumption held by poorest 20 percent	...	...	...	...	...
Population below $1 a day (percent)	...	...	...	...	...
Population below minimum level of dietary energy consumption (percent)	...	...	...	...	...
Poverty gap ratio at $1 a day (incidence x depth of poverty)	...	...	...	...	...
Poverty headcount, national (percent of population)	...	...	...	...	...
Prevalence of underweight in children (under five years of age)	...	...	...	...	...
Goal 2: Achieve universal primary education					
Net primary enrollment ratio (percent of relevant age group)	...	...	*82.9*	79.3	*81.3*
Primary completion rate, total (percent of relevant age group)	...	...	*93*	98	*91*
Percentage of cohort reaching grade 5 (percent)	75.4	...	...	85.4	...
Youth literacy rate (percent ages 15−24)	...	...	...	...	...
Goal 3: Promote gender equality and empower women					
Proportion of seats held by women in national parliament (percent)	10.0	...	9.0	9.0	19.0
Ratio of girls to boys in primary and secondary education (percent)	...	...	*103.2*	102.5	*100.3*
Ratio of young literate females to males (percent ages 15−24)	...	...	...	...	...
Share of women employed in the nonagricultural sector (percent)	...	...	...	...	...
Goal 4: Reduce child mortality					
Immunization, measles (percent of children ages 12−23 months)	88	99	99	99	99
Infant mortality rate (per 1,000 live births)	19	*17*	...	14	12
Under 5 mortality rate (per 1,000)	23	20	...	16	14
Goal 5: Improve maternal health					
Births attended by skilled health staff (percent of total)	...	...	...	*99.9*	...
Maternal mortality ratio (modeled estimate, per 100,000 live births)	...	...	...	...	...
Goal 6: Combat HIV/AIDS, malaria, and other diseases					
Contraceptive prevalence rate (percent of women ages 15−49)	...	...	*50*	...	...
Incidence of tuberculosis (per 100,000 people)	19.3	18.1	17.3	16.5	15.7
Number of children orphaned by HIV/AIDS	...	...	...	...	...
Prevalence of HIV, total (percent of population aged 15−49)	...	...	...	...	...
Tuberculosis cases detected under DOTS (percent)	...	...	84.2	...	*35.5*
Goal 7: Ensure environmental sustainability					
Access to an improved water source (percent of population)	...	...	...	...	97.0
Access to improved sanitation (percent of population)	...	...	...	...	83.0
Access to secure tenure (percent of population)	...	...	...	...	...
CO2 emissions (metric tons per capita)	0.8	1.0	1.1	1.4	...
Forest area (percent of total land area)	66.7	...	...	61.3	...
GDP per unit of energy use (2000 PPP $ per kg oil equivalent)	...	...	...	...	...
Nationally protected areas (percent of total land area)	...	...	...	...	...
Goal 8: Develop a global partnership for development					
Aid per capita (current US$)	272.8	237.2	202.2	213.5	153.5
Debt service (percent of exports)	6.0	7.0	7.0	7.0	13.0
Fixed line and mobile phone subscribers (per 1,000 people)	163.8	228.0	263.4	309.8	423.9
Internet users (per 1,000 people)	...	*5.1*	*26.4*	77.8	*160.3*
Personal computers (per 1,000 people)	...	...	..	71.3	*89.7*
Unemployment, youth female (percent of female labor force ages 15−24)	...	...	46.3	...	...
Unemployment, youth male (percent of male labor force ages 15−24)	...	...	36.4	...	...
Unemployment, youth total (percent of total labor force ages 15−24)	...	...	40.6	...	...

Source: World Development Indicators database, April 2005.

1/ The goals, targets, and relevant indicators to assess progress over the period from 1990 to 2015 when targets are expected to be met, are explained in **http://millenniumindicators.un.org/unsd/mi/mi_goals.asp** and **http://ddp-ext.worldbank.org/ext/MDG/home.do**

2/ Figures in italics refer to periods other than those specified.

Dominica: Fund Relations

(As of August 31, 2005)

I. Membership Status Joined 12/12/78; Article VIII

II. General Resources Account	**SDR Million**	**Percent of Quota**
Quota	8.20	100.00
Fund holdings of currency	11.16	136.15
Reserve position in Fund	0.01	0.11

III. SDR Department	**SDR Million**	**Percent of Allocation**
Net cumulative allocation	0.59	100.00
Holdings	0.04	7.36

IV. Outstanding Purchases and Loans:	**SDR Million**	**Percent of Quota**
PRGF Arrangements	4.21	51.28
Stand-By Arrangements	2.97	36.25

V. Latest Financial Arrangements:

Type	**Approval Date**	**Expiration Date**	**Amount Approved** (SDR Million)	**Amount Drawn** (SDR Million)
PRGF	12/29/03	12/28/06	7.69	4.21
Stand-by	08/28/02	01/02/04	2.97	2.97
SAF	11/26/86	11/25/89	2.80	2.80
Stand-by	07/18/84	07/17/85	1.40	0.97
EFF	02/06/81	02/05/84	8.55	8.55

Projected Payments to the Fund on an Obligation Basis (SDR Million)[12]:

			Forthcoming		
	2005	**2006**	**2007**	**2008**	**2009**
Principal	0.26	1.10	1.23	0.38	0.50
Charges/Interest	0.04	0.13	0.08	0.05	0.04
Total	**0.30**	**1.23**	**1.31**	**0.43**	**0.54**

VI. Exchange rate arrangement: Dominica is a member of the Eastern Caribbean Currency Union, which has a common central bank (the Eastern Caribbean Central Bank) and

[12] Based on existing use of resources and present holdings of SDRs.

currency (the Eastern Caribbean dollar). Since July 1976, the Eastern Caribbean dollar has been pegged to the U.S. dollar at the rate of EC$2.70 per U.S. dollar.

VII. **Safeguards Assessment**: Under the Fund's safeguards assessment policy, the Eastern Caribbean Central Bank (ECCB), of which Dominica is a participating government, is subject to a full safeguards assessment. The on-site safeguards assessment was completed on February 20, 2003, and concluded that the ECCB has in place appropriate mechanisms to manage resources, including Fund disbursements and that the vulnerabilities that remain do not present an undue risk. The safeguards assessment proposed specific measures to address these vulnerabilities, which have been substantially implemented by the ECCB.

VIII. **Article IV consultation**: The last Article IV consultation was concluded by the Executive Board on August 28, 2002; the relevant documents are IMF Country Report No. 02/223 and IMF Country Report No. 02/224. Dominica is on a 24-month cycle.

IX. **Technical assistance:** An **MFD mission** recently visited Roseau to provide technical assistance in strengthening the supervisory framework for AML/CFT in the nonbank sector. **FAD missions** have provided technical assistance on tax policy and administration, most recently on VAT implementation, on urban property taxation (1997), and on tax policy and administration, and expenditure control (1995). Technical assistance from MFD and FAD has complemented the assistance that has been provided by the Caribbean Regional Technical Assistance Center (CARTAC) in Barbados.

X. **FSAP:** A joint IMF/World Bank team performed an assessment of the financial sector of the member states of the ECCB, in two missions—September 1–19 and October 20–31, 2003. The principal objective of the missions was to assist the authorities in assessing the development needs and opportunities for the financial sector and identifying potential vulnerabilities of financial institutions and markets to macroeconomic shocks, as well as the risks to macroeconomic stability from weaknesses and shortcomings in the financial sector. The Financial System Stability Assessment (FSSA) was discussed by the Executive Board on May 5, 2004, and subsequently published on the IMF's external website, including the Report on the Observance of Standards and Codes (ROSC) on Banking Supervision.

Dominica: World Bank Relations[13]

(As of August 31, 2005)

The World Bank role in Dominica: The Bank will continue to collaborate with the Fund and other donors in supporting the authorities efforts in stabilizing macroeconomic conditions and in restarting economic growth and reducing poverty. The Bank will lead the policy dialogue on key structural reforms, including public investment, social protection, and on the environment for private sector development.

Bank-Fund collaboration in specific areas: The World Bank and the IMF will continue to collaborate on the financial sector, on the medium-term structural reform agenda and in providing technical assistance to Dominica on macroeconomic management issues jointly with the Caribbean Regional Technical Assistance Center (CARTAC).

Bank Group strategy: The World Bank's strategy for Dominica is a part of the Country Assistance Strategy (CAS) for the Eastern Caribbean (OECS) sub-region, presented to the Bank Board on June 4, 2001. The CAS which covers FY 2002–06, proposes new commitments of around US$110 million for the five borrowing member states of the OECS (Dominica, Grenada, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines). The main goals of the strategy are to reduce income insecurity and vulnerability at the national and household levels, and build human and institutional capacity to meet the challenging economic and social environment facing these small states.

Ongoing projects: There are currently two ongoing World Bank projects in Dominica (as well as other OECS borrowing countries) with total commitments of approximately US$7.5 million.

(i) The *OECS Telecommunications Reform Program*, approved in FY 1998 seeks to introduce pro-competition reforms in the telecommunications sectors and increase the supply of informatics-related skills in the OECS borrowing countries. The project has helped these countries establish a regional regulatory authority, negotiate with the sub-regional telecommunications monopoly, and lower telephone rates. Dominica's share of the US$6.0 million loan is US$1.2 million.

(ii) The *OECS Emergency Recovery Project*: This project was approved in FY 2002 to help mitigate the impact of the September 11 events on the tourism sector. The project supports improvements to airport and sea port security arrangements. The World Bank's assistance for this sub-regional program is US$21 million, including US$3.2 million for Dominica.

[13] Source: World Bank.

Negative pledge update: Dominica remains ineligible for new Bank lending operations in light of the apparent violation of its negative pledge clauses under the earlier IBRD loans. The government continues to make efforts to resolve this issue.

Analytical and advisory services: The Bank has recently prepared a number of analytical reports for Dominica including a Country Financial Accountability Assessment, Social Protection Review, a Country Procurement Assessment, and a Public Expenditure Review. The Bank is also providing technical assistance to support public sector reforms and actions in the petroleum, electricity and financial sectors.

Key aspects of the Bank's Caribbean research and technical assistance program include:

(i) a recently completed study of Growth and Competitiveness in the OECS;
(ii) a recently completed FSAP in collaboration with the IMF;
(iii) an ongoing study of energy options in the OECS; and
(iv) a review of the relationship between poverty and the environment.

Financial Relations: Gross Disbursements and Debt Service During Fiscal Year
(In millions of U.S. dollars)

	1998	1999	2000	2001	2002	2003	2004	2005*
Total disbursements	1.9	1.4	2.1	0.5	1.7	2.7	4.0	…
Repayments	0.1	0.1	0.1	0.1	0.1	0.3	0.6	…
Net disbursements	1.8	1.3	1.9	0.4	1.6	2.3	3.4	…
Cancelled	0.0	0.0	0.0	0.0	1.0	2.3	0.0	…
Interest and fees	0.1	0.1	0.2	0.3	0.3	0.3	0.4	…

* Data for 2004 are projections.

Dominica: Relations with the Caribbean Development Bank (CDB)

(As of August 31, 2005)

CDB has approved loans totaling US$143.7 million, of which US$10.1 million are undisbursed. In July 2004, CDB approved exceptional financial assistance of a US$6.4 million grant in support of Dominica's stabilization and reform program, as well as a combination of interest rate reduction and extension of maturities on existing concessionary loans. The total operation resulted in a reduction in Dominica's debt service estimated at US$13.2 million in NPV terms as at June 30, 2004.

Major projects

1. ***Seventh Consolidated Line of Credit***—to assist DAIDB in continuing to finance its lending programme in the following areas: Agricultural and Industrial Credit, Housing and Student Loans. US$7.0 million is approved and US$1.5 million is undisbursed.

2. ***Upgrading of Ecotourism Sites***—the construction of access roads and reception centres, related infrastructure as well as site trails at five major tourism sites across the island. US$3.1 million is approved and US$0.6 million is undisbursed

3. ***Student Loan Scheme (Seventh Loan)***—to provide DAIDB with resources to continue financing its student loan programme. US$7.0 million is approved and US$3.0 million is undisbursed.

4. ***Shelter Development Project***—to establish a framework for developing the shelter sector on a sustainable basis with particular reference to low-income households. US$2.3 million is approved and US$1.6 million is undisbursed.

5. ***Roseau Water and Sewerage Project***—to provide for the rehabilitation and extension of the existing Roseau sewerage system, the provision of pre-treatment facilities, a marine outfall, the replacement of the central Roseau potable water distribution system and a partial upgrade of the water supply system. US$10.0 million was approved and disbursed.

6. ***OECS Solid Waste Management Project***—the upgrading of dump sites into sanitary landfills; procurement of equipment for the collection and transportation of waste; management of special wastes; improvement of storage facilities for domestically generated waste and promotion of waste recovery and recycling activities. US$1.4 million is approved and US$1.1 million is undisbursed.

7. ***Caribbean Court of Justice***—to provide for the establishment and operation of a final Court of Appeal to replace the Judicial Committee of the Privy Council and to act as a final arbiter in disputes arising between CARICOM member states or between a CARICOM national and another country. US$2.2 million was approved and disbursed.

Dominica: Loan Disbursement

(In millions of U.S. dollars)

	2001	2002	2003	2004	2005[1]
Net disbursement	10.50	3.66	8.46	10.39	1.29
Disbursement	13.20	6.25	11.26	20.61	2.32
Amortization	2.70	2.59	2.80	10.22	1.03
Interest and charges	1.76	1.90	2.03	2.25	1.20
Net resource flow	8.74	1.76	6.43	8.14	0.09

[1] As at June 30, 2005.

Dominica: Statistical Issues

Dominica's statistical database is inadequate for both meeting the authorities' needs and Fund surveillance. There are weaknesses in coverage, accuracy and reliability, frequency, and timeliness that continue to frustrate effective economic analysis and policy formulation. The weakest areas are the fiscal accounts, public debt, and the balance of payments.

The authorities are aware of the deficiencies in their statistical database and started participation in the General Data Dissemination System (GDDS) in September 2000. Metadata and plans for improving the statistical system are posted on the IMF's Dissemination Standards Bulletin Board (http://dsbb.imf.org).

Real sector

CPI data are provided on a timely basis. The Eastern Caribbean Central Bank (ECCB) compiles semi-annual GDP estimates, which are available with a one-quarter lag. Estimated annual data on nominal GDP as well as at constant prices of 1990 (by activity) are available within a few months of the end of the year. Data on employment are very limited and there are no official data on producer prices or wages in the private sector. Results of the 2001 population census have not yet been published.

Government finance

Statistical capacity problems affect the timely production of quality government finance statistics. In particular, the data are subject to frequent revisions stemming in part from omissions and misclassifications. Data on central government operations are incomplete and must be supplemented with additional information from external sources. For instance, some operations are undertaken outside the consolidated fund. These include certain investment spending, loan and grant receipts, and on-lending and transfers to public enterprises. As a result, capital expenditure data, recorded by the Treasury, must be supplemented with additional donor financing information, particularly because the Public Sector Investment Program (PSIP) data are not timely. Delays in the reporting of the PSIP data reportedly stem from reporting delays from the line ministries.

The authorities do not provide consolidated nonfinancial public sector data; data for the rest of the public sector—Dominica Social Security and the public enterprises—must be obtained directly from each entity during Fund Article IV consultation missions.

In addition, only limited financing data are available. Although much progress has been made in improving the measurement of the government's debt, there are concerns that there is still some under-recording of government commitments. However, there are several ongoing initiatives to strengthen expenditure management, which should help minimize the extent of this problem. In particular, there is an ongoing effort to automate the expenditure execution process. The new automation technology will be fully installed in all line ministries in 2004, at which point all local purchase orders (LPOs) will be entered and tracked electronically. Automatic commitments will be charged against a specific budget allocation once LPOs are generated electronically. All ministries and suppliers of goods and services will be compelled to use the new system following the completion of the automation program.

No government finance data are reported to STA for publication in the *International Financial Statistics* (*IFS)* or the *Government Finance Statistics* (*GFS) Yearbook*.

The authorities have been receiving technical assistance from the United Kingdom's Department for International Development (DIFID) on the cash management system and from CARTAC on monitoring implementation of the stabilization program and treasury accounting.

Monetary statistics

Monetary statistics are compiled by the ECCB on a monthly basis and reported to the Fund regularly, although the coverage merits improvements. For instance, the banking statistics do not explicitly capture loans from ECCB's fiscal reserve tranche to the government. The monetary survey does not include the accounts of credit unions that accept demand deposits. The ECCB is aware of the need to improve coverage of the monetary statistics and is taking steps to collect data on credit unions. Data on the activities of offshore banks are not reported to the Fund.

Balance of payments

Balance of payments data are compiled by the ECCB on an annual basis and are not reported in the format recommended in the fifth edition of the IMF's *Balance of Payments Manual*. The timeliness of the data has improved recently but the data still suffer from exceptionally high and volatile errors and omissions, at times reaching levels of 12 percent of GDP.

External debt

The ministry of finance maintains a database on public and publicly-guaranteed external loans that provides detailed and reasonably current information on disbursements, debt service, and debt stocks. The Treasury maintains the data on bonds placed abroad. Unfortunately, the two government agencies do not consolidate their databases to provide a comprehensive external debt picture. The external debt data are deficient with the result that debt stock cannot be accurately measured. Monthly information on payments by creditor (actual and scheduled) is not fully and readily available, which impedes the compilation of up-to-date information on arrears.

Dominica: Table of Common Indicators Required for Surveillance

(As of September 14, 2005)

	Date of latest observation	Date received [7]	Frequency of Data [7]	Frequency of Reporting [7]	Frequency of publication [7]
Exchange Rates[1]	Fixed Rate	NA	NA	NA	NA
International Reserve Assets and Reserve Liabilities of the Monetary Authorities [1, 2]	June 2005	8/25/05	M	M	Q
Reserve/Base Money	Jul. 2005	8/22/05	M	M	Q
Broad Money	Jul. 2005	8/22/05	M	M	Q
Central Bank Balance Sheet	June 2005	8/19/05	M	M	Q
Consolidated Balance Sheet of the Banking System	Jul. 2005	8/15/05	M	M	Q
Interest Rates[3]	June 2005	8/15/05	Q	Q	Q
Consumer Price Index	July 2005	8/25/05	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[4] – General Government[5]	2004	06/10/05	A	A	A
Revenue, Expenditure, Balance and Composition of Financing[4] – Central Government	Jul. 2005	8/24/05	M	M	A
Stocks of Central Government and Central Government-Guaranteed Debt[6]	Jul. 2005	8/24/05	M	M	A
External Current Account Balance	2004	03/15/05	A	A	A
Exports and Imports of Goods and Services	June 2005	08/24/05	M	Q	A
GDP/GNP	2004	03/15/05	A	A	A
Gross External Debt	Jul. 2005	8/24/05	M	M	A

[1] Dominica is a member of the Eastern Caribbean Currency Union, in which the common currency of all member states (E.C. dollar) is pegged to the U.S. dollar at US$1=EC$2.70.
[2] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[3] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[4] Foreign, domestic bank, and domestic nonbank financing.
[5] The general government consists of the central government and state and local governments.
[6] Currency and maturity composition are provided annually.

Roseau, Dominica
September 8, 2005

Mr. Rodrigo de Rato,
Managing Director,
International Monetary Fund
700 19th Street, NW,
Washington, DC 20431
USA

Dear Mr. de Rato,

1. It has been more than a year and a half since Dominica requested an arrangement under the Fund's Poverty Reduction and Growth Facility (PRGF) to cope with the economic crisis that had emerged and resolve our fiscal and debt difficulties. The government outlined its economic policies in the letter of intent and memorandum of economic policies (MEP) of December 10, 2003 and redefined them subsequently in the context of the programme reviews.

2. Performance under the programme remains satisfactory. All quantitative performance criteria for end-June 2005 were met, except for the performance criterion on nonobservance of external payments arrears. An external debt service payment on a government-guaranteed loan was inadvertently delayed for a few days due to an operational error by the borrowing institution. Government has made progress in structural reforms and all the structural benchmarks for the fifth review were implemented. We have also made considerable progress in the collaborative restructuring our debt, and will continue our good faith efforts to reach agreements with our nonparticipating creditors.

3. Dominica remains committed to the arrangement under the PRGF and the attached supplementary MEP outlines our policies for FY 2005/2006. The proposed indicative targets, performance criteria, and structural benchmarks are indicated in Tables 1 and 2. On this basis, we request a waiver for the nonobservance of the continuous performance criteria on external payments arrears, completion of the fifth review of the programme and the release of the associated disbursement under the arrangement.

4. We also request the extension of repurchase expectations arising in the one-year period commencing on December 22, 2005 totaling an amount equivalent to SDR 1,268,444. We believe that meeting these repurchase expectations would impose undue hardship and

risk at a crucial time, and we therefore request instead that these repurchases be made on an obligations basis starting on December 22, 2006.

5. The Government of Dominica will provide the Fund with such information as the Fund may request in connection with progress in implementing the economic and financial policies, and achieving the objectives of the programme. The government believes that the policies set out in the attached MEP are adequate to achieve the objectives of the programme, but it will take further measures that may become necessary for this purpose. We will consult with the Fund on the adoption of these measures, and in advance of revisions to the policies contained in the MEP, in accordance with the Fund's policies on such consultation. We authorize the Fund to publish this letter and the attached supplement to our MEP to facilitate a wider access to our policies and signal the seriousness of our commitment to the programme to civil society and the international community.

Sincerely,

/s/

Honourable Roosevelt Skerrit
Prime Minister and Minister of Finance and Planning

Attachment

SUPPLEMENT MEMORANDUM OF ECONOMIC POLICIES OF THE GOVERNMENT OF DOMINICA

I. BACKGROUND

1. Our economy continues to recover from the economic crisis and financial disarray in 2001–02 triggered by the build-up of public debt to unsustainable levels. Reflecting the comprehensive economic reforms that the Government of the Commonwealth of Dominica has pursued in the last few years, public finances are on a firmer footing and economic growth has recovered—with output expansion set to exceed the historical average for the second straight year in 2005.

2. **Sustaining the improved growth performance to better the standard of living of all Dominicans remains the central objective of our economic policies**. To this end, our economic reform strategy retains its four elements, with the emphasis now decidedly shifting to the policies necessary to sustain high economic growth. Specifically:

- With creditor participation in our **collaborative debt restructuring** past 70 percent, our objective is to try to reach agreement with all remaining nonparticipating creditors;
- Our **fiscal stance** will be consistent with reducing the public debt burden to sustainable levels;
- **Fiscal reforms** are being undertaken to improve the transparency and effectiveness of the tax regime and the budgetary process; and
- Critically, we are also determined to improve the **enabling environment for private sector investment**, which will require measures to enhance the efficiency of the public service and re-orient our public sector investment programme towards the provision of physical and human capital investment.

II. PERFORMANCE UNDER THE PROGRAMME

3. **Macroeconomic outcomes were strong in 2004 and the first half of 2005**. Output growth in 2004, estimated at some 3½ percent, was broad-based, with transportation, agriculture, manufacturing and construction all showing signs of a robust recovery from the 2001–02 slump. This rebound in activity was mirrored in a sharp rebound in credit growth, which had been contracting since early 2001, but accelerated sharply last year to an annual growth of 7 percent. While inflation has been somewhat volatile in recent months, it nonetheless averaged 1½ percent in 2004. Export growth has remained modest at some 9 percent in 2004, while imports have surged reflecting the economic recovery and higher energy prices. The same broad trends are evident in developments in the first half of this year.

4. **All but one performance criteria for the fifth review have been met.** Reflecting one-off revenues which contributed to arrears reduction and lower spending on goods and services, end-March 2005 indicative targets were met with large margins as were all end-June quantitative performance criteria. The primary balance in FY 2004/05 was 4.4 percent of GDP, about 2½ percent above the target notwithstanding the fact that unexpected one-off expenditures related to the Caribbean Court of Justice and emergency reconstruction costs following last November's earthquake had to be accommodated into the budget. The margin on the wage bill performance criterion was smaller at less than EC$1 million. However, due to a technical glitch, there was a temporary delay (about a week) in debt service payment by DOMLEC on a government guaranteed loan causing the continuous performance criteria on nonaccumulation of external arrears to be unobserved.

5. **All three structural benchmarks for the fifth review under the programme have been now been observed**:

- The on-site inspection of the Roseau Cooperative Credit Union was completed on schedule. Concerns about the level of nonperforming assets, account-handling practices, and the quality of the audit process were flagged.

- Amendments to the Finance Administration Act for Cabinet and public discussion were prepared in May. Proposals for numerical targets were prepared separately in August, and submitted to Cabinet with the amendments. Public consultation began in September.

- The 2005/06 budget was approved by Parliament on August 4, with a primary balance target consistent with the programme.

6. **We are also making considerable progress in identifying and implementing other structural reforms**.

- The Government of Dominica has decided to publish in the Official Gazette all Cabinet decisions granting new tax and duty concessions—a step that will enhance the transparency of public finances. Concessions granted in 2004/05 were sent to the publishers in August. Going forward, publication will occur on a monthly basis (with a one month lag). The published material will identify the beneficiary of the tax exemption as well as the legal basis for the concession.

- In the area of public expenditure management, the main government account is now being reconciled on a monthly basis. In addition, all transactions conducted are now being captured in the general ledger, and opening balances will be adjusted by end-December. Moreover, all local purchase orders are now generated electronically.

- In an effort to strengthen the accountability and financial management of public enterprises and statutory bodies and ensure greater reporting to the general public, we will submit to Parliament the audited financial accounts for the year ending in 2004 for AID Bank, DOWASCO, and DEXIA by end-2005. The accounts for the NDC are being prepared for audit by end-December and will be submitted to Parliament early in 2006. We will continue this practice going forward.

- With the help of an IMF/World Bank technical assistance mission, a review of the financial condition of Dominica Social Security (DSS) was completed in June. The study shows that the pension system's finances are on a highly unsustainable trajectory. However, the study also identified reforms that, if implemented promptly, can address the very large threat to public finances.

7. **We remain committed to engaging our creditors in good faith negotiations**. We have signed agreements with all our domestic creditors, including DSS (see below). As a sign of our commitment to making good faith efforts to reach agreement with remaining external nonparticipating creditors, we continue to make payments on the new restructured terms into an escrow account on their behalf. We also expect to shortly pass legislation to allow the debentures that we have issued to the creditors that participated in the restructuring to be traded on the Eastern Caribbean Stock Exchange (ECSE).

III. Enabling Growth and Reducing Vulnerabilities

8. **The government is in the process of finalizing its growth and social protection strategy (GSPS) paper to guide our policies over the medium term**. The growth strategy seeks to make the private sector the engine of economic growth, with the government playing a facilitating role. The social protection aspects will focus on reducing the vulnerabilities during the period of adjustment.

9. **The key growth sectors will be tourism, energy, services, agriculture, light manufacturing, and offshore education**. The potential for heritage, health, and ecotourism is largely untapped; we will focus on improvement of related infrastructure and product development, which will facilitate private sector investments. We are working with potential investors to tap our geothermal resources, to satisfy both export and domestic demand. We expect a substantial lowering of the cost of electricity over the medium term as this project develops, which would help spur light manufacturing, including agro-processing. On agriculture, the development of the tourism sector and the agro-processing sub sector should lead to increased demand for agricultural produce. We also hope to target niche markets, including in the region, for agricultural exports. There is also potential for further development of offshore educational institutions and linking them further with the domestic economy. The recent liberalization of the telecommunications sector has created potential for the development of related services. On this basis, we expect the economy to grow at around 3 percent per annum over the medium term. This should allow us to make inroads towards lowering unemployment and consequently reduce the incidence of poverty. In the short term, however, we intend to strengthen the social safety nets by ensuring better targeting.

10. **Consistent with the broad strategy laid out in the GSPS, the government's programme to improve the enabling environment for increased private sector activity includes several important initiatives for the immediate period ahead**.

- We intend to obtain parliamentary approval (by end-December, 2005) of amendments to the Electricity Supply Act and related legislation with a view to demonopolizing the sector to inter alia allow new entrants, establish a regulatory commission, and put in place a tariff structure more reflective of production costs and other economic circumstances. Beyond strengthening the regulatory framework for electricity supply, these changes are important to attract investors to exploit our substantial geo-thermal energy capacity—the exploitation and export of such electricity would, in addition to helping boost growth, provide foreign exchange earnings, and reduce vulnerabilities to high oil prices.

- To improve the effectiveness of the financial sector and ensure its viability is sustained, we will take the necessary steps by end-October 2005 to allow the FSU (with external technical assistance), to conduct an on-site inspection of AID Bank (by end-March 2006). Relatedly, a memorandum of understanding has been signed with the Roseau Cooperative Credit Union (RCCU) to address the issues identified during the recent on-site inspection. The FSU will ensure that these measures are adopted by end-December to bring the RCCU in full regulatory compliance.

- There is a need to redefine the role of the public sector outside of the central government, to realign it towards the requirements of private sector-led growth and ensure high quality of public services. To this end, plans are under way to complete strategic reviews and establish action plans (by end-December 2005) for the operations of the AID Bank, DEXIA and NDC, with a view to enhancing their efficiency, streamlining their functions and improving accountability. The reviews will consider the justification for the continued existence of all of these three agencies in an environment where the government's role in the growth process is to provide a supportive environment for the private sector. An important objective of these reforms is a one-stop shop that will streamline the process and shorten the time required for establishing businesses—to be put in place by end-March 2006.

- We recognize the need to reduce red tape in order to encourage investments, including from the Dominican Diaspora. We continue to consider additional ways in which the Diaspora can contribute to the development of Dominica. We are in the process of streamlining paperwork and other requirements related to the importation of goods into Dominica. We will also make such requirements transparent by publishing them in government websites.

IV. THE 2005/06 BUDGET

11. **The macroeconomic framework underpinning our budget assumes growth will be sustained at 3 percent this year and next**. These rates of growth are higher than the

historical average, but not unduly optimistic taking into account the spare capacity in the economy and the expected boost to activity from higher public sector investment. Inflation is expected to remain subdued at 1½ percent in 2005/06.

12. **Further debt consolidation is an important pillar of our macroeconomic policies**. The 2005/06 budget targets a primary surplus of 3 percent of GDP, broadly in line with that realized in 2004/05 and consistent with reducing our high debt burden to sustainable levels over the medium term. A still higher primary balance would be prudent given our country's vulnerability to natural disasters—as last November's earthquake attests—and the need to prepare for the steep increase in pension costs projected for the coming years. But this needs to be weighed against the near-term investments needs. The 3 percent primary surplus for 2005/06 and beyond strikes the appropriate balance.

13. **The budget is underpinned by a number of revenue and expenditures measures, including:**

- As announced in the budget speech, the VAT is expected to come into effect on March 1, 2006. The switch from the consumption and sales taxes to VAT is expected to be revenue neutral, but with substantial benefits in terms of expanding the tax base and economic efficiency.

- As originally legislated, the 5 percent cut in civil servants wages imposed at the outset of the stabilization programme has been restored in the 2005/06 budget. This would imply a wage bill of some 13.7 percent of GDP, which is very high even by the standards of other small island economies. Accordingly, measures are being taken to avoid the wage bill crowding-out other essential and productive expenditures and adjusting the wage scale over time to allow the government to retain and attract more highly qualified personnel (see below).

- To make the state college financially independent over time, starting in FY 2005/06, the college is being treated as an independent entity from the budget, with financial support limited to an explicit transfer. The plan is to make the college rely increasingly on nonbudgetary sources of funding.

- The public sector investment programme (PSIP) will be kept to a level consistent with our implementation capacity, and focused on projects that will yield the highest rates of return.

- We will use budget-support grants in excess of programmed amounts to pay down our debt and build up bank balances. The next review will reassess the outlook for revenues and expenditures and revisit the fiscal programme targets as appropriate.

V. Structural fiscal reforms

14. **Large unfunded liabilities in the pension system are a major threat to public finances**. Reflecting population aging, the number of pensioners per contributor is expected to increase sharply from 0.23 in 2004 to 0.32 in 2020 and 0.78 by 2050. The net present value (NPV) of the unfunded liabilities of DSS are estimated at more than 150 percent of GDP. The restructuring of the government's debt has also had the effect of further weakening the financial position of DSS. Therefore, in the absence of corrective measures, cash flows will turn negative in 2014 and DSS will deplete its reserves by 2025. The transfers that the central government would need to make to fill the gap between DSS's income and spending would mean that public finances would return to an unsustainable path.

15. **The government recognizes that reforms to address the financial problems in DSS are unavoidable.** Ultimately, the choice is not between reform and no reform, but between gradual, moderate, and equitable reform now or abrupt, drastic, and inequitable reforms later when the pension system's finances are exhausted. Accordingly, we will prepare an action plan (by end-December 2005) to eliminate the unfunded liabilities of DSS that will identify specific steps and a time line for implementation, and we will subsequently have this plan approved by Cabinet (by end-March 2006). Putting the finances of the DSS on a sustainable footing will require adjustments to: the replacement rate, the contribution rate, the number of years over which average earnings are calculated, and the retirement age. The reform strategy will consider the appropriate balance between these options. Another important reform objective is international diversification of DSS's portfolio, which we will be undertaken in a gradual manner. In the interim, we have regularized the financial relations between the government and DSS, including by finalizing the debt restructuring agreement in September 2005.

16. **The overriding objective for the public sector is for our country to have a relatively smaller, more efficient, and better paid public service—consistent with our vision of the private sector playing the dominant role in the economy**. To that end, we intend to reduce the role of the government, with particular attention to the share of the wage bill in GDP.

- For 2005/06, the government has adopted a number of measures to initiate the process of focusing the civil service on the core activities that the government needs to provide. These measures include outsourcing of janitorial and government building protection services and streamlining the airport and ports authorities. Government is hopeful that the initial (redundancy) costs of this exercise will be grant-financed from the EU's Framework of Mutual Obligations. Steps are also being taken to reduce overtime pay at Customs. These initiatives will ensure that the allocation for the wage bill will be adhered to.

- Second, as outlined in the budget, in addition to the foregoing measures, the government will keep under review the scope for streamlining, commercializing or privatizing other services. The government has already identified possible additional measures. The overall objective of these initiatives is to reduce the wage bill further by 1–1½ percent of GDP from its current level of 13¾ percent of GDP over the next three years. With this in mind, the on-going review by the Establishment, Personnel and Training Division on public service reform will continue, with a view to streamlining the structure and functioning of government ministries and departments. This review, which will be completed by end-February, will *inter alia* seek to address unfilled positions, with a view to identifying and eliminating those that are no longer necessary.

- Third, future wage and salary increases will be consistent with progress in reaching the objectives of reducing the wage bill. The government recognizes the need to improve emoluments of deserving civil servants, and expects that further rationalization of public sector employment will contribute to this.

17. **Further reforms are also being put in place to strengthen the framework governing public finances.** Based on the outcome of the public and Cabinet discussions of the proposed revisions to the Finance Administration Act (FAA), we plan to obtain Cabinet approval of the amendments to the FAA by end-November 2005 and parliamentary approval in early 2006. These amendments to the FAA will improve the credibility of fiscal policy, provide an anchor for public expectations regarding the public finances over the medium term, as well as improve the transparency and accountability of the management of public finances. Specifically:

- The revised legislation will outline as an important objective the reduction of public debt to prudent levels. It will further note that the government will target a primary surplus consistent with reducing public debt annually while the debt stock remains above 60 percent of GDP—the benchmark recommended by the ECCB. Where such a primary surplus is not being targeted, the government, in its annual budget document, will need to provide a comprehensive explanation of the reasons for the deviation from the target and outline its policies for getting back on target within the shortest possible timeframe.

- Moreover, these amendments will be buttressed by a public commitment by the government to aim for a 3 percent of GDP primary surplus in the budget. Again, where a primary surplus of at least 3 percent is not being targeted, the government, will provide a comprehensive explanation of the reasons for the deviation from the target and outline its policies for getting back on target within the shortest possible timeframe.

18. **Further reforms are planned to improve the consistency of budget and debt management**. With the help of CARTAC, we intend to introduce medium-term budgeting practices for line ministries to minimize ad hoc shifts in the fiscal stance and instill a greater measure of expenditure controls. To ensure debt remains sustainable and off-budget entities do not accrue excessive liabilities, we have adopted guidelines under which the government is willing to extend guarantees.

19. **Preparations for the introduction of a VAT on March 1, 2006 continue apace**. The draft VAT and Excise Tax Laws are expected to be approved by Parliament in August (prior action), with implementing regulations finalized soon after. The VAT will have two rates (a standard 15 percent rate and a 10 percent rate for hotel accommodation), and zero rating and exemptions have been kept to a minimum. To ensure the VAT will be introduced on time, organizational and staffing issues have been resolved and IT infrastructure will be tested and put in place by end-October 2005. All necessary steps will be taken to ensure that the introduction of VAT refunds can be made on a timely basis.

20. **The government also intends to undertake a comprehensive review of statutory tax exemptions**. The review will by end-December consider the justification for statutory and nonstatutory concessions, and repeal those that are found to be unnecessary.

21. **The government will continue to closely monitor the projects that are included in the Public Sector Investment Programme (PSIP) for their consistency with our growth and poverty reduction strategy.** The PSIP for the 2005/06 budget is broadly in line with the our poverty reduction strategy document—the Growth and Social Protection Strategy (GSPS) paper. To ensure full consistency with the GSPS, government will seek to ensure an appropriate balance between investments in the economic sectors and economic and social infrastructure. The government will strictly limit nongrant financed capital spending to a level that is consistent with agreed macroeconomic parameters. Consistent with our implementation capacity, we will also limit the overall PSIP to around 10 percent of GDP.

Table 1. Dominica: Quantitative Performance Criteria and Indicative Targets Under the PRGF, September 2005–June 2006 1/

	2005		2006	
	Sept. 30 Program 2/	Dec. 31 Program 2/	Mar. 31 Program 2/	June 30 Program 2/
I. Performance Criteria (PC)				
(In millions of Eastern Caribbean dollars)				
Central government primary balance	2.9	7.6	16.2	23.7
Central government wage bill	27.6	55.7	81.4	106.5
Banking system net credit to central government	3.0	-0.1	-6.4	-13.6
Net changes in central government arrears to private domestic parties	4.0	8.0	8.0	8.0
(In millions of U.S. dollars)				
Disbursement of central government or central government guaranteed external nonconcessional debt with maturity of at least one year	1.9	4.4	6.9	9.0
Net changes in the outstanding stock of short-term external debt contracted or guaranteed by the central government (with maturity of less than one year) 3/	0.0	0.0	0.0	0.0
Nonaccumulation of central government and central government guaranteed external payments arrears 3/ 4/	0.0	0.0	0.0	0.0
II. Indicative Targets (IT)				
(In millions of Eastern Caribbean dollars)				
Central government overall balance	-10.5	-14.0	-18.7	-19.3
Central government revenues	52.9	111.1	171.9	230.8
Central government primary savings	5.5	14.0	27.3	38.9

Sources: Dominican authorities; and Fund staff estimates and projections.

1/ All variables and any adjustors that apply, are defined in the Technical Memorandum of Understanding.

2/ Cumulative amounts from June 30, 2005. Targets for September 31, 2005 and March 31, 2006 are all indicative targets.

3/ These performance criteria will be monitored on a continuous basis.

4/ Waiver requested for the external arrears known at the time of the Executive Board discussion on October 14, 2005.

Table 2. Structural Conditionality

(Structural benchmarks, unless otherwise indicated)

Prior Actions for the Fifth Review

- Passage by Parliament and enactment into law of a VAT Act with an effective date of March 1, 2006.
- Approval by Cabinet of an implementation plan to rationalize the wage bill.

Sixth Review

- Establish legislative basis for the Financial Services Unit (FSU) to supervise insurance companies and regulate all nonbank financial institutions, including the Agriculture and Industrial Development Bank (end-December, 2005).
- Complete strategic review and establish action plans for the operations of Aid Bank, DEXIA and NDC, with a view to enhancing their efficiency, streamlining their functions and improving accountability (end-December, 2005).
- Parliamentary approval of amendments to the Electricity Supply Act and related legislation (end-December 2005).
- Complete review by end-February 2006 the streamlining of the structure and functioning of government ministries and departments, with a view to further reducing wage bill over the following three years.
- Implementation of VAT starting March, 1 2006 (**structural performance criterion**).

Seventh Review

- Cabinet approval of action plan to eliminate the unfunded liabilities of DSS (end-March 2006).
- Parliamentary approval of amendments to the Finance Administration Act as described in paragraph 17 (end-May, 2006).
- Line ministries to submit rolling three-year expenditure plans (end-May, 2006).

TECHNICAL MEMORANDUM OF UNDERSTANDING

1. Dominica's performance under the Poverty Reduction and Growth Facility (PRGF), described in the letter of the Government of Dominica dated September 8, 2005, will be assessed by the IMF on the basis of the observance of quantitative performance criteria as well as compliance with structural performance criteria and benchmarks. This Technical Memorandum of Understanding (TMU) sets out and defines the quantitative performance criteria, indicative targets, and benchmarks specified in Tables 1 and 2 of the Supplement Memorandum of Economic Policies (SMEP), as well as the monitoring and reporting requirements.

2. The Dominican authorities are committed to transmit to the Fund staff the best data available. All revisions or expectations thereof shall be promptly reported to the Fund staff.

3. The variables mentioned herein for the purpose of monitoring the performance criteria, which are not explicitly defined, are consistent with the Government Financial Statistics (GFS). For variables omitted from the TMU which are relevant for the program targets, the authorities of Dominica shall consult with the Fund staff on their appropriate treatment, based on GFS principles and Fund program practices.

I. FISCAL TARGETS

A. Indicative Target on the Overall Balance of the Central Government

4. The **central government overall balance** will be measured from the financing side as the sum of the net domestic borrowing plus net external borrowing.

5. **Net domestic financing** by the central government is the sum of: (i) net domestic bank financing as measured by the change in the domestic banking system credit to the central government net of deposits, as reported by the consolidated balance sheet of the monetary authorities[14] and commercial banks, including special tranches from the ECCB and excluding net changes in (a) "double signature accounts"[15] and (b) the deposits of the cash grants from the People's Republic of China; (ii) net nonbank financing as measured by the net changes in holdings of government securities by nonbanks, and net borrowing from nonbank institutions; (iii) the change in the stock of domestic arrears of the central

[14] Consolidating the ECCB's balance sheet (excluding the government's IMF operating account) and the government's transactions with the IMF.

[15] The "double signature accounts" include the accounts 115002797, 115002976,115002220, 115001912, 115003051, 115001911, 115003025, 115001471, 115001523, 115003053, 115001710, and 100038724 held in the National Bank of Dominica (NBD), and any new account in which grant receipts are deposited and which requires a signature of an external party for the release of its funds. It is expected that the forthcoming grants from the European Union in late 2005 will be released through a "double signature account."

government defined as net changes in unpaid checks issued, unprocessed claims, pending invoices, plus accrued interest payments, and other forms of expenditures recorded above the line but not paid; (iv) gross receipts from divestment; (v) financing from debt restructuring measured as domestic debt service payments (principal and interest) on a due basis less actual debt service payments; and (vi) any other exceptional financing.[16]

6. **Net external financing** of the central government is defined as the sum of (i) disbursements of project and nonproject loans, including securitization, but excluding the use of IMF resources; (ii) proceeds from bonds issued abroad; (iii) exceptional financing (rescheduled principal and interest), net changes in cash deposits held outside the domestic banking system, (iv) net changes in short-term external debt; (v) any change in arrears on external interest payments and other forms of external expenditures recorded above the line but not paid; (vi) financing from debt restructuring measured as external debt service payments (principal and interest) on a due basis less actual debt service payments; (vii) any other exceptional financing; and less (viii) payments of principal on current maturities for bonds and loans on a due basis but excluding the use of IMF resources, and including any prepayment of external debt.

7. The programmed amounts of debt service on a due basis are shown in Table 1 below:

Table 1. Domestic and External Debt Service Payments on a Due Basis

	External Interest Payments	External Amortization Payments	Domestic Interest Payments	Domestic Amortization Payments
(In millions of Eastern Caribbean dollars)				
Cumulative flows (from June 30, 2005)				
End-September 2005	8.3	3.2	5.1	0.9
End-December 2005	11.5	13.2	10.1	1.7
End-March 2006	19.7	16.1	15.2	2.9
End-June 2006	22.8	20.4	20.2	3.5

[16] Treasury bills will be recorded at face value, except for those held by the banking system which will be recorded on a purchase price basis.

The program floors on the overall balance are reported in Table 2 below.

Table 2. Indicative Target on the Overall Balance of the Central Government

	(In millions of Eastern Caribbean dollars)
Cumulative balance (from June 30, 2005)	
End-September 2005 (indicative target)	-10.5
End-December 2005 (indicative target)	-14.0
End-March 2006 (indicative target)	-18.7
End-June 2006 (indicative target)	-19.3

8. The floor on the overall balance of the central government will be adjusted as follows:

(i) Upward[17] to the extent that **budgetary grants** exceed programmed amounts. Budgetary grants are defined as grant receipts that are not earmarked for capital outlays, and including the drawdown of deposits of the cash grants from China. For the purpose of this adjustor, the programmed budgetary grants for fiscal year 2005/06 amount to: EC$2.6 million by end-September 2005; EC$3.8 million by end-December 2005; EC$5.0 million by end-March 2006; and EC$6.2 million by end-June 2006.[18]

(ii) Downward by the amount severance payments and the administrative expenditures linked to the debt restructuring operations exceed the grants targeted to these programs.

(iii) Upward by the amount received from Security Bond forfeitures.

B. Performance Criterion on the Central Government Primary Balance

9. **The central government primary balance** is defined as the central government overall balance (from the financing side as defined in paragraph 4) plus domestic and external interest payments on a due basis. Interest payments do not include either domestic or external interest payments made by the central government on behalf of other parties.

10. The program floors on the central government primary balance are reported in Table 3 below.

[17] Upward adjustment means lower deficit.

[18] The program assumes that EC$4.8 million will be received from EU STABEX 1998/99/00 to cover severance payments and other already identified projects.

Table 3. Performance Criterion on the Central Government Primary Balance

	(In millions of Eastern Caribbean dollars)
Cumulative balance (from June 30, 2005)	
End-September 2005 (indicative target)	2.9
End-December 2005 (performance criterion)	7.6
End-March 2006 (indicative target)	16.2
End-June 2006 (performance criterion)	23.7

11. The same adjustors described in paragraph 9 apply to the primary balance.

Performance Criterion on the Central Government Wage Bill

12. The **central government wage bill** will be measured as the total expenditure of the central government on wages and salaries of central government employees net of wage refunds, including acting allowances, special duty allowances, responsibility allowances, subsistence allowances, the employer contribution to Dominica Social Security, but not including retirement benefits, severance payments or other related one-off payments (i.e., accumulated leave). As such, the ceiling does not include wage-related transfers to schools, the National Development Corporation, and local governments.

13. The program ceilings on the central government wage bill are shown in Table 4 below:

Table 4. Performance Criterion on the Central Government Wage Bill

	(In millions of Eastern Caribbean dollars)
Cumulative flows (from June 30, 2005)	
End-September 2005 (indicative target)	27.6
End-December 2005 (performance criterion)	55.7
End-March 2006 (indicative target)	81.4
End-June 2006 (performance criterion)	106.5

C. Performance Criterion on the Central Government Arrears Accumulation to Domestic Private Parties

14. **Net changes in central government arrears to domestic private parties** is defined as changes in the sum of all pending payments by government for goods and services already purchased from these parties, as well as pending unpaid checks for payments into the escrow account set up for debt restructuring. Private domestic parties exclude DOWASCO, Dominica Social Security, National Development Corporation, Dominica Broadcasting Corporation, DEXIA, and the Ports Authority. The measure used will be unpaid checks issued and pending invoices for which payment is overdue.

15. The program ceilings on the central government arrears accumulation to domestic private parties are reported in Table 5 below.

Table 5. Performance Criterion on the Central Government Arrears Accumulation to Domestic Private Parties

	(In millions of Eastern Caribbean dollars)
Cumulative flows (from June 30, 2005)	
End-September 2005 (indicative target)	4.0
End-December 2005 (performance criterion)	8.0
End-March 2006 (indicative target)	8.0
End-June 2006 (performance criterion)	8.0

D. Indicative Targets on Revenues of the Central Government

16. **Central government revenues** are defined as the tax collections and nontax revenues reported in the treasury accounts (economic classification), excluding: (i) revenues from the economic citizenship program, (ii) foreign and domestic grant receipts, (iii) repayment of loans, (iv) wage refunds, and (v) privatization receipts, and includes income tax refunds. Capital revenues are excluded.

17. The program floors on the revenues of the central government are reported in Table 6 below.

Table 6. Indicative Targets on Revenues of the Central Government

	(In millions of Eastern Caribbean dollars)
Cumulative flows (from June 30, 2005)	
End-September 2005 (indicative target)	52.9
End-December 2005 (indicative target)	111.1
End-March 2006 (indicative target)	171.9
End-June 2006 (indicative target)	230.8

E. Indicative Targets on the Primary Savings of the Central Government

18. **Central government primary savings** is measured on an accrual basis (including unpaid checks issued and unprocessed invoices) and is defined as the central government revenue before grants (i.e., excluding grants) minus current noninterest expenditure. The adjustors described in paragraph 9 apply to the central government primary savings.

19. The program ceilings on the central government primary savings are reported in Table 7 below.

Table 7. Indicative Targets on the Primary Savings of the Central Government

	(In millions of Eastern Caribbean dollars)
Cumulative flows (from June 30, 2005)	
End-September 2005 (indicative target)	5.5
End-December 2005 (indicative target)	14.0
End-March 2006 (indicative target)	27.3
End-June 2006 (indicative target)	38.9

Monitoring discretionary tax exemptions

20. **Discretionary tax exemptions** are defined as tax exemptions granted under Sections 6(2) and 31 of the Consumption Order Act, Section 26 of the Sales Tax Act, Section 60 of the Customs (Control and Management) Act, Section 25(2) of the Income Tax Act, or remissions of tax under Section 109 of the Income Tax Act (except in cases where the Comptroller certifies that the tax to be remitted is uncollectible).

21. The number of discretionary tax exemptions will be monitored on a continuous basis.

II. Monetary Targets

A. Performance Criterion on the Net Credit of the Banking System to the Central Government

22. **Net credit of the banking system** is defined as in paragraph 5. The program ceilings on the net credit of the banking system to the central government are reported in Table 8 below.

Table 8. Performance Criterion on the Net Credit of the Banking System to the Central Government

	(In millions of Eastern Caribbean dollars)
Cumulative flows (from June 30, 2005)	
End-September 2005 (indicative target)	3.0
End-December 2005 (performance criterion)	-0.1
End-March 2006 (indicative target)	-6.4
End-June 2006 (performance criterion)	-13.6

23. The ceiling on net credit of the banking system will be adjusted upward (downward) to the extent that actual interest payments are higher (lower) than the programmed amounts on a cash basis. The programmed amounts of interest payments on a cash basis are shown in Table 9 below.

Table 9. Interest Payments on a Cash Basis

	Total Interest Payments	Domestic Interest Payments	External Interest Payments
(In millions of Eastern Caribbean dollars)			
Cumulative flows (from June 30, 2005)			
End-September 2005	5.0	2.7	2.3
End-December 2005	8.8	4.5	4.3
End-March 2006	13.9	7.2	6.6
End-June 2006	17.8	9.1	8.7

III. External Sector Targets

A. Performance Criterion on Disbursements of Nonconcessional External Central Government or Central Government Guaranteed Debt with Maturity of at Least One Year

24. Disbursements of nonconcessional external central government and central government guaranteed debt with maturity of at least one year will be monitored by the Accountant General's office on a monthly basis. Central government and central government guaranteed debt is defined to include debt contracted or guaranteed by the central government.

25. The program ceilings on disbursements of nonconcessional external central government or central government guaranteed debt with maturity of at least one year are reported in Table 10 below.

Table 10. Performance Criterion on Disbursements of Nonconcessional External Central Government or Central Government Guaranteed Debt with Maturity of at Least One Year

	(In millions of U.S. dollars)
Cumulative flows (from June 30, 2005)	
End-September 2005 (indicative target)	2.6
End-December 2005 (performance criterion)	6.7
End-March 2006 (indicative target)	8.3
End-June 2006 (performance criterion)	10.0

26. The term **"debt"** is defined as set forth in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274-(00/85), August 24, 2000):

"(a) For the purpose of this guideline, the term "debt" will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows:

> (i) loans, i.e., advances of money to obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans, and buyers' credits) and temporary exchanges

of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);

(ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until some time after the date on which the goods are delivered or services are provided; and

(iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lesser retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair or maintenance of the property.

(b) Under the definition of debt set out in point 21(a) above, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt."

27. **Nonconcessional debt** is defined as debt having a grant element (in net present value relative to face value) **of less than 35 percent**, based on the currency- and maturity-specific Commercial Reference Rates (CIRR), published monthly by the OECD.[19] The limit excludes the disbursements of short-term import-related debts, the use of Fund resources, and refinancing operations.

B. Performance Criterion on the Net Changes in the Outstanding Stock of Short-Term External Debt with Original Maturity of Less than One Year Contracted or Guaranteed by the Central Government

28. The **stock of short-term external debt outstanding** is defined as debt with original maturity of less than one year contracted or guaranteed by the central government. The term debt is defined as set forth in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274-(00/85), August 24, 2000) (see paragraph 27 above), but excludes normal import-related credits.

[19] For loans with a maturity of at least 15 years, the 10-year average commercial interest reference rates and for loans with shorter maturities, the 6-month average CIRRs, as of August 2005 published by the OECD will be used as the discount rates. To both the 10-year and 6-month averages, the following margins for differing repayment periods will be added: 0.75 percent for repayment periods of less than 15 years; 1 percent for 15–19 years; 1.15 percent for 20–29 years; and 1.25 percent for 30 years or more.

29. No short-term external debt with original maturity of less than one year, will be contracted or guaranteed by the central government. This ceiling will be monitored on a continuous basis.

C. Performance Criterion on Nonaccumulation of Central Government and Central Government Guaranteed External Payment Arrears

30. **Central government and central government guaranteed external payment arrears** are defined as overdue payments (principal or interest) on debt contracted or guaranteed by the central government. The definition of external payment arrears under the program **excludes**: (i) debt claims that were irrevocably tendered in the debt exchange closed on September 31, 2005 (the "Debt Exchange”), (ii) debt claims that were eligible to participate in the Debt Exchange but have not been tendered, and (iii) debts claims of official bilateral creditors which are under rescheduling or refinancing negotiation. It also does not include outstanding subscription payments to regional and international organizations, for which understandings will be reached to ease payment obligations consistent with the program.

31. No external payment arrears of the central government and central government guaranteed debt, will be allowed in the program. This ceiling will be monitored on a continuous basis.

IV. STRUCTURAL CONDITIONALITY

(Structural benchmarks unless otherwise indicated)

Prior Actions for the Fifth Review

- Passage by Parliament and enactment into law of a VAT Act with an effective date of March 1, 2006.
- Approval by Cabinet of an implementation plan to rationalize the wage bill.

Sixth Review

- Establish legislative basis for the Financial Services Unit (FSU) to supervise insurance companies and regulate all nonbank financial institutions, including the Agriculture and Industrial Development Bank (end-December, 2005).
- Complete strategic review and establish action plans for the operations of Aid Bank, DEXIA and NDC, with a view to enhancing their efficiency, streamlining their functions and improving accountability (end-December, 2005).
- Parliamentary approval of amendments to the Electricity Supply Act and related legislation (end-December 2005).
- Complete review by end-February 2006 the streamlining of the structure and functioning of government ministries and departments, with a view to further reducing wage bill over the following three years.
- Implementation of VAT starting March, 1 2006 (**structural performance criterion**). This is understood to mean that the first tax period for which the VAT law would apply starts on March 1, 2006 or earlier.

Seventh Review

- Cabinet approval of action plan to eliminate the unfunded liabilities of DSS (end-March 2006).
- Parliamentary approval of amendments to the Finance Administration Act as described in paragraph 17 of the SMEP (end-May, 2006).
- Line ministries to submit rolling three-year expenditure plans (end-May, 2006).

V. Periodic Reporting

32. **Regular reporting on a monthly basis** (and when possible weekly) will include the following:

- Data for monitoring the program's performance criteria and monthly indicative targets, including

  - Fiscal sector

    (i) Central government budgetary accounts.

    (ii) Dominica Social Security Balance Sheet, showing amounts receivable from central government for contributions and interest.

    (iii) Central government domestic debt data.

    (iv) Current grant inflows.

    (v) Stock of unpaid checks issued and stock of unprocessed claims due and invoices pending.

    (vi) Capital expenditure (project by project) and composition of financing, including revised projections for the remainder of the fiscal year.

    (vii) Balances in the debt servicing account linked to the Royal Merchant Bank Bond Issue.

    (viii) Total number of exemptions issued (by type of exemption).

    (ix) Severance payments and administrative expenditures linked to the debt restructuring operations, and details about how they were financed.

  - Financial sector

    (x) Monetary survey for Dominica as prepared by the Eastern Caribbean Central Bank, including balances in central government double signature accounts.

  - External and real sectors

    (xi) Imports and exports data by product.

(xii) Detailed (creditor by creditor) external debt report from the Debt Unit in the Ministry of Finance and Planning, showing fiscal year-to-date disbursements, amortization, interest payments, and outstanding stocks, for the central government, public enterprises and AID Bank.

(xiii) Total disbursements/grant receipts, monthly, disaggregated into: (a) budgetary support (by type—either loans or external "bonds" and/or other securities); (b) project loans; (c) budgetary grants; and (d) project grants.

(xiv) Stock of external payment arrears of the NFPS, including amortization and interest payment arrears, and supplier arrears for the central government, public enterprises, and AID Bank.

(xv) Copies of loan agreements for any new loans contracted, including financing involving the issue of government paper, and of any renegotiated agreements on existing loans.

(xvi) Consumer price index.

(xvii) Real sector indicators.

All information will be reported to Fund staff within three weeks of the end of each month.

33. Reporting **on an annual basis** will include the following:

- External and real sectors

(xviii) GDP and its components.

(xix) Balance of payments accounts.

34. Other reporting will include:

- Reports of legislative changes pertaining to economic matters.

Dominica: Public Debt Sustainability Analysis

1. This section assesses the sustainability of Dominica's public debt using the debt sustainability analysis (DSA) template for low-income countries. The DSA was conducted jointly by Fund and Bank staff.

2. Based on the analysis in the baseline scenario and several alternative scenarios, the staff conclude that while Dominica's public debt is sustainable at current output growth rates and fiscal stance, there are risks of future debt distress if these variables weakened. In addition, the deficits that Dominica's social security system (DSS) is expected to face starting in 2014 pose another challenge to the country's public finances.

Dominica's public debt situation at end-2004

3. Dominica initiated a collaborative debt restructuring process in 2004 with a view to reducing its debt to a more sustainable level. Following discussions with creditors, the restructuring targeted an NPV to face value reduction of 50 percent. So far, creditors with about 70 percent of the debt eligible for restructuring have agreed to the proposal, and the authorities remain in good faith negotiations with the remaining hold-out creditors.

4. It is assumed that those creditors not currently participating in the restructuring receive the intermediate bond. In addition, external interest arrears are excluded since arrears with participating creditors have been settled as part of the debt restructuring and arrears with nonparticipating creditors are either in dispute or expected to be settled when an agreement is reached. Undisputed interest arrears amount to approximately 0.4 percent of GDP.

5. As of end of 2004 and after taking into account the restructuring, Dominica had a public debt of around 116 percent of GDP, with external public debt reaching around 81 percent of GDP. The net present value to GDP ratios stood at approximately 90 percent for the total public debt and 54 percent for the external. Around 47 percent of GDP is owed to multilateral creditors (with the Caribbean Development Bank holding almost two thirds of this). External debt with bilateral creditors is approximately 19 percent of GDP while debt to commercial creditors is around 16 percent of GDP). With respect to domestic debt, about 15 percent of GDP is owed to Dominica's Social Security System (DSS) and 20 percent of GDP is owed to commercial banks, the ECCB, and corporations.

The baseline scenario

6. The baseline scenario is developed for 2005–2025 and refers to the public debt of the nonfinancial public sector. The main assumptions are:

- GDP growth stays at 3 percent. While this assumption implies a rate of growth higher than the average observed in the 1990s (2 percent), it seems consistent with the stronger growth observed in 2004 and first half of 2005 and with growth recorded before the 1990s. In addition, this rate of growth seems achievable given the improved macro policy environment, as well as the structural reforms envisioned in the draft Growth and Social Protection Strategy document (which is close to being finalized) and the favorable prospects for the tourism sector.

- The primary balance of the central government remains at 3 percent of GDP over the projection period, while pubic enterprises run an overall deficit of 0.5 percent of GDP. The assumption about the government primary balance is consistent with the strong fiscal turnaround Dominica has had in recent years and with the target that the government has committed to maintain under the program. The assumption on public enterprises follows the average observed during the period 1999–2004.

- Annual disbursements of external concessional debt reach 1.5 percent of GDP, which is consistent with the projections of the country's public sector investment program (PSIP).

- New domestic financing can be obtained by the central government and public enterprises at an interest rate of 7 percent.

7. Under the baseline scenario (Table 1a), all the indicators of debt burden show that Dominica's debt remains sustainable. The only indicator that does not decline continuously is the debt service to revenue ratio, which temporarily shows an upward trend and then a decline starting in 2014.[20] While the increase in the ratio of debt service to revenue is temporary, the high debt servicing costs point to the need of maintaining fiscal discipline in order to avoid liquidity constraints.

8. Under this scenario, Dominica would reach a public debt to GDP ratio of 60 percent by 2018.

Sensitivity analysis

Changes in growth and primary balance scenarios

9. The sensitivity analysis illustrates two important points (Table 2a). First, if Dominica primary balance and economic growth return to their averages of the last ten years (a 1 percent of GDP primary deficit and 0.8 percent growth), then public debt turns unsustainable (case described in Scenario A.1). Second, if Dominica can keep the fiscal effort it made during last year (a primary surplus of around 4.3 percent of GDP), then public debt remains sustainable (Scenario A.2).

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[20] The initial upward trend is mainly caused by two features of the debt restructuring. First, the grant extended by the CDB covers interest payments and amortization of several of the loans Dominica has with that institution in 2005 and 2006, which makes the debt service to GDP low in those years. Second, Dominica's debt restructuring includes a repurchase clause which is expected to increase amortization starting in 2009.

10. In addition, the sensitivity analysis shows the importance of sustaining growth at current levels. In the alternative Scenario A.3 in which growth falls to 2½ percent per year, most indicators of debt burden present a slight upward trend. Behind this adverse effect of growth on the debt burden is the fact that as output growth slows, fiscal revenues would also likely decline, causing the primary balance to deteriorate. As the interest rate on new nonconcessional financing (7 percent) is much larger than Dominica's current average interest rate (around 2.8 for external debt and 5 percent for domestic debt), this scenario also increases interest expenditures over time.

Social Security

11. Dominica Social Security (DSS) is currently running surpluses, but deficits are expected to emerge starting in 2014 and grow continuously over time. At the request of the Dominican authorities, a World Bank/FAD technical assistance mission visited the country in June 2005 to assess the financial situation of DSS and propose possible reforms.

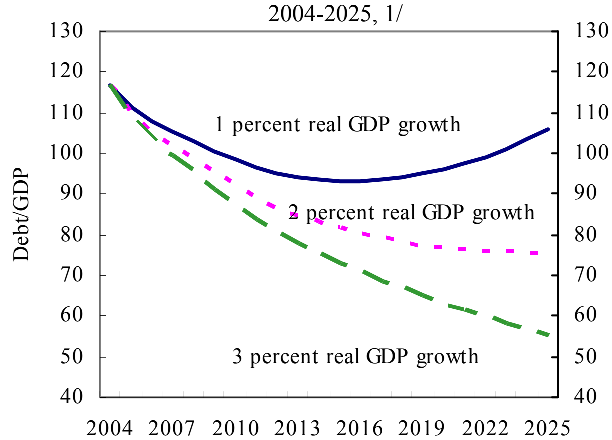
12. While the projected deficits in the social security system are expected to be addressed through structural reforms, a scenario on the implications of direct transfers from the central government on the debt path in absence of reforms was also considered. The exercise assumes that the government starts making transfers in 2014 in order to cover DSS' deficits. Under this scenario, public debt to GDP initially declines (reaching around 60 percent in 2020) but then starts to increase again as DSS deficits become larger over time.

Changes in interest rates

13. Given that Dominica's debt to GDP ratio is still high, the implication of adverse changes in interest rates was also considered.

14. Chart 1a describes the path of the public debt to GDP ratio assuming the interest rates available for new financing reaches 12 percent (5 percentage points above the baseline scenario) and different growth rates. As can be seen in the graph, public debt remains sustainable when the other key variables remain under the baseline assumptions (i.e., 3 percent GDP growth and 3 percent primary surplus) although its decline is much slower than in the baseline scenario. When GDP growth declines to 2 percent, then public debt stabilizes at around 75 percent of GDP at the end of the projection period. With a GDP growth of 1 percent, public debt would return to an unsustainable path.

Chart 1.a. Dominica: Public Sector Debt to GDP 2004-2025, 1/



1/ Assumes 3 percent primary surplus by the Central Government. Excludes the impact of DSS deficits and abstracts from natural disasters. The interest rate for new financing is assumed to be 12 percent, which is five percentage points above the baseline assumption.

Natural disasters

15. The impact of natural disasters can be analyzed using the stress tests provided in Table 2a. For instance, the fifth bound test presented in Table 2a suggests that Dominica's debt would remain sustainable after a natural disaster that increased the debt to GDP ratio by 10 percent in 2006.[21]

[21] Given the variability of the impact of natural disasters, it is difficult to determine the appropriate magnitude for this test. However, the ECCU Selected Issues Paper from 2004, looks at a sample of 12 large natural disasters occurring in the ECCU since 1970 and reports a median public debt increase of 6.5 percent of GDP over a period of three years after the disaster. The shock presented here is larger than what would be suggested by the previous evidence.

Table 1a.Dominica: Public Sector Debt Sustainability Framework, 2002-2025
(In percent of GDP, unless otherwise indicated)

	Actual					Estimate	Projections								
	2002	2003	2004	Historical Average 5/	Standard Deviation 5/	2005	2006	2007	2008	2009	2010	Average 2005-2010	2015	2025	Average 2011-2025
Public sector debt 1/	127.2	130.6	116.7			109.1	103.9	99.5	95.3	91.1	87.1		69.4	39.7	
o/w foreign-currency denominated 7/	79.9	84.4	81.2			81.1	77.6	72.9	68.5	64.2	58.7		39.7	23.1	
Change in public sector debt	33.6	3.4	-13.9			-7.6	-5.2	-4.4	-4.3	-4.2	-4.0		-3.3	-2.9	
Identified debt-creating flows 8/	11.0	-2.6	-11.6			-7.6	-5.0	-4.4	-4.3	-4.2	-4.1		-3.3	-3.0	
Primary deficit	1.2	-6.1	-4.4	0.9	4.5	-3.3	-3.3	-3.3	-3.3	-3.2	-3.2	-3.3	-3.1	-3.1	-3.1
Revenue and grants	41.2	49.9	48.8			47.5	47.3	47.2	47.1	47.1	47.1		47.1	47.1	
of which : grants	4.5	9.2	6.1			8.3	8.3	8.3	8.3	8.3	8.3		8.3	8.3	
Primary (noninterest) expenditure	42.4	43.9	44.5			44.2	44.0	43.8	43.8	43.9	43.9		44.0	44.0	
Automatic debt dynamics	9.8	3.5	-1.7			-1.8	-1.7	-1.1	-1.1	-1.0	-0.9		-0.2	0.1	
Contribution from interest rate/growth differential	9.1	3.2	-2.3			-2.4	-2.2	-1.5	-1.4	-1.3	-1.2		-0.4	0.0	
of which : contribution from average real interest rate	4.5	3.2	2.1			1.0	1.0	1.5	1.5	1.4	1.4		1.7	1.2	
of which : contribution from real GDP growth	4.6	0.0	-4.4			-3.4	-3.2	-3.0	-2.9	-2.8	-2.7		-2.1	-1.2	
Contribution from real exchange rate depreciation	0.7	0.3	0.6			0.6	0.4	0.4	0.4	0.3	0.3		...	...	
Other identified debt-creating flows	0.0	0.0	-5.6			-2.5	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0			-2.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	-0.9			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other) 6/	0.0	0.0	-4.6			-0.6	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	22.6	5.9	-2.4			0.0	-0.2	0.1	0.1	0.1	0.1		0.1	0.1	
NPV of public sector debt	...	...	90.0			83.3	79.9	77.7	75.4	73.2	70.9		59.3	34.0	
o/w foreign-currency denominated	...	...	54.6			55.3	53.6	51.1	48.7	46.2	42.5		29.7	17.4	
o/w external	...	...	54.6			55.3	53.6	51.1	48.7	46.2	42.5		29.7	17.4	
NPV of external debt in percent of exports	...	...	115.0			111.8	108.2	102.9	97.9	92.7	85.0		59.4	34.8	
External debt service in percent of exports	11.8	19.5	20.8			6.1	8.4	10.0	9.6	9.5	11.9		7.2	3.8	
NPV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	7.0	4.6	2.6			1.8	2.6	3.1	3.0	4.0	5.8		3.7	1.8	
NPV of public sector debt-to-revenue ratio (in percent) 3/			184.4			175.5	169.1	164.8	160.2	155.4	150.5		126.0	72.2	
o/w external			111.7			116.5	113.5	108.4	103.5	98.2	90.2		63.1	37.0	
Debt service-to-revenue ratio (in percent) 3/ 4/	14.2	21.3	14.3			10.6	12.5	13.7	13.3	15.3	19.1		14.4	10.4	
Primary deficit that stabilizes the debt-to-GDP ratio	-32.4	-9.4	9.6			4.3	1.9	1.0	1.0	0.9	0.8		0.2	-0.2	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	-4.7	0.0	3.5	0.9	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
Average nominal interest rate on forex debt (in percent)	5.0	3.9	4.0	3.7	1.0	2.1	2.1	2.8	2.7	2.7	2.7	2.5	2.8	3.2	2.9
Average real interest rate on domestic currency debt (in percent)	8.0	3.3	1.4	6.1	3.0	3.5	3.7	3.8	3.8	3.7	3.8	3.7	4.6	5.4	4.7
Real exchange rate depreciation (in percent, + indicates depreciation)	1.0	0.4	0.7	0.3	1.0	0.8	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	0.6	1.5	1.4	1.5	0.8	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5
Growth of real primary spending (deflated by GDP deflator, in percent)	6.0	4.5	5.0	2.7	11.4	2.1	2.5	2.5	2.8	2.9	2.9	2.6	2.9	2.8	2.9
Grant element of new external borrowing (in percent)	...	...	...			35.6	35.6	35.6	35.6	35.6	35.6	35.6	35.6	35.6	...

Sources: Country authorities; and Fund staff estimates and projections.
1/ Non-financial Public Sector (includes debt with Dominica's Social Security System)
2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.
3/ Revenues including grants.
4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.
5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.
6/ In 2004, it is assumed that all nonparticipating creditors received the intermediate bond, which carries a face value reduction of 20 percent.
7/ Refers to external debt. Assumes that nonpartcipating creditors receive the intermediate bond. Excludes external interest arrears.
Arrears with participating creditors have been settled as part of the debt restructuring. Arrears with nonparticipating creditors
are either in dispute or expected to be settled when an agreement is reached. Undisputed interest arrears are approximately 0.4 percent of GDP
8/ Fiscal year aggregates presented on a fiscal year basis

Table 2a.Dominica: Sensitivity Analysis for Key Indicators of Public Debt 2005-2025

	Estimate	Projections						
	2005	2006	2007	2008	2009	2010	2015	2025
NPV of Debt-to-GDP Ratio								
Baseline	83	80	78	75	73	71	59	34
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	83	86	90	94	99	104	133	229
A2. Primary balance is unchanged from 2004	82	78	74	71	67	63	43	-8
A3. Permanently lower GDP growth 1/	83	81	79	78	77	76	75	94
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2006-2007	83	86	92	94	96	98	109	140
B2. Primary balance is at historical average minus one standard deviations in 2006-2007	83	89	95	94	92	90	80	54
B3. Combination of B1-B2 using one half standard deviation shocks	83	89	97	95	92	90	75	38
B4. One-time 30 percent real depreciation in 2006	83	104	102	100	98	95	81	45
B5. 10 percent of GDP increase in other debt-creating flows in 2006	83	90	88	86	84	83	74	55
NPV of Debt-to-Revenue Ratio 2/								
Baseline	175	169	165	160	155	150	126	72
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	175	181	190	198	207	216	272	449
A2. Primary balance is unchanged from 2004	173	164	158	150	143	135	91	-17
A3. Permanently lower GDP growth 1/	175	170	168	165	163	161	158	197
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2006-2007	175	181	192	196	200	204	227	295
B2. Primary balance is at historical average minus one standard deviations in 2006-2007	175	187	202	199	195	191	170	115
B3. Combination of B1-B2 using one half standard deviation shocks	175	188	204	199	194	188	159	81
B4. One-time 30 percent real depreciation in 2006	175	220	216	212	207	202	173	96
B5. 10 percent of GDP increase in other debt-creating flows in 2006	176	190	187	183	180	176	157	116
Debt Service-to-Revenue Ratio 2/								
Baseline	11	12	14	13	15	19	14	10
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	11	13	17	19	23	29	33	61
A2. Primary balance is unchanged from 2004	11	12	12	12	13	17	10	-2
A3. Permanently lower GDP growth 1/	11	13	14	14	16	20	19	27
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2006-2007	11	13	16	18	22	27	27	40
B2. Primary balance is at historical average minus one standard deviations in 2006-2007	11	12	20	23	21	24	19	16
B3. Combination of B1-B2 using one half standard deviation shocks	11	13	20	22	20	23	17	11
B4. One-time 30 percent real depreciation in 2006	11	13	16	16	18	21	16	10
B5. 10 percent of GDP increase in other debt-creating flows in 2006	11	12	21	17	18	22	18	16

Sources: Country authorities; and Fund staff estimates and projections.

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of 20 (i.e., the length of the projection period).

2/ Revenues are defined inclusive of grants.

Roseau, Dominica
September 8, 2005

Mr. Rodrigo de Rato,
Managing Director,
International Monetary Fund
700 19th Street, NW,
Washington, DC 20431
USA

Dear Mr. de Rato,

The attached report outlines the status of the Government of the Commonwealth of Dominica's growth and social protection strategy paper which is expected to be finalized before the end of this year.

Sincerely,

/s/
Honourable Roosevelt Skerrit
Prime Minister and Minister of Finance and Planning

Attachment

Dominica—Preparation Status Report of Growth and Social Protection Strategy

Introduction

The Government of the Commonwealth of Dominica (GOCD) submitted its Interim Poverty Reduction Strategy Paper (I-PRSP) to the Boards of the IMF and the World Bank in December of 2003. In that document, the government presented an assessment of the poverty situation in Dominica, and outlined an interim medium- and long-term strategy to tackle it.

The Executive Boards of both the World Bank and the International Monetary Fund, as well as the staffs of the two institutions have given us valuable feedback on our interim strategy paper. In particular, the Joint Staff Assessment emphasized the need for a more detailed analysis of the structural reforms needed in Dominica and highlighted the importance of maintaining macroeconomic stability. Staffs also suggested involving the large Dominican Diaspora in the consultation process.

Status of the Poverty Reduction Strategy Paper

At the time the paper was submitted, it was envisaged that our Growth and Social Protection Strategy (GSPS) would be finalized by the end of 2004. While we have made substantial progress in developing many of the areas outlined in the I-PRSP and issues raised in the consultation process, the GSPS has not yet been completed.

While recognizing the advantages of having a finalized poverty reduction strategy in place, the GOCD has considered it important that additional time be taken-up to finalize the report for two reasons. First, the government expects the GSPS to guide its policies over the medium term and, in consequence, wants it to cover all of the areas that are relevant for its reform agenda. Second, given the importance of the document, we have decided to undertake an extensive consultation process. Following a series of focus group discussions earlier in the year, we have also discussed the GSPS at a donors meeting held in June 2005.

At this stage, we are the in process of finalizing GSPS, and expect to submit the document to the Boards of the Bank and Fund by the end of this year.

Issues Raised in Joint Staff Assessment

The GSPS tries to address many of the issues that were raised in the staff's joint assessment:

- In the area of macroeconomic stability, we have taken measures to improve the primary balance and sought collaborative debt restructuring, helping put public finances on a firmer footing.

- Fiscal structural reforms that we are currently considering include amendments to the Finance Administration Act which will ensure fiscal responsibility in the future. We have also recently passed legislation that will allow the introduction of a Value Added Tax in March of 2006. Reforms are also being taken on the expenditure side, where we continue to rationalize public wages.

- The government has advanced its sectoral strategy to enhance growth in several dimensions. For instance, the country now has a national tourism policy which will set the policy agenda in the medium term. With technical assistance from the World Bank, the government has been reviewing its Electricity Supply Act in order to modify it and allow the exploitation of geothermal energy, which potentially can be exported to neighboring islands. The government is also overseeing the development of a water industry in Dominica, with the potential to export bulk and bottled water.

- The government has also made progress in the area of social protection. For instance, with technical assistance from the IMF and the World Bank, the government is currently assessing how to tackle the unfunded liabilities of the social security system, which will start to run deficits starting in 2014 as population aging puts pressure on the system. The government has also analyzed more carefully the problematic of HIV/AIDS in the country and the situation of the Carib community. The government strategy to deal with these two issues will be presented in the final GSPS.

- The final version of the GSPS will contain a much more detailed structural reform agenda than the one envisaged in the I-PRSP. This reflects the considerable emphasis the government is putting to the country's structural reform as well as the result of the consultation process and technical assistance provided by international organizations and donors.

New timeline

Having now reviewed the recommendations from the extensive consultation process in the first half of 2005, we feel comfortable that the GSPS can be finalized shortly, and on the outside by the end of the year.

Public Information Notice (PIN) No. 05/149
FOR IMMEDIATE RELEASE
October 25, 2005

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2005 Article IV Consultation with Dominica

On October, 14, 2005, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Dominica.[1]

Background

Dominica is recovering from the aftermath of an economic and financial crisis in 2001–02 when output contracted by 10 percent. The crisis originated in the expansionary fiscal policies of the preceding decade, when the authorities sought to prop-up activity by increasing public spending. The primary balance of the central government turned strongly negative in the mid-1990s, public debt quickly reached unsustainable levels, and financing constraints soon led to a rapid accumulation of mostly domestic arrears. By 2001, financing was available only at precipitously high interest rates and the government faced a major liquidity crisis. Additionally, the adverse effects of a severe drought on agriculture and the September 2001 terrorist attacks on the nascent tourism sector, precipitated a steep recession.

Dominica has come a long way from the low-point of the crisis. In mid-2002, the government initiated a stabilization program aimed at ensuring an orderly adjustment, strengthening public finances and implementing measures to reinvigorate growth. With the debt-to-GDP ratio approaching 130 percent, the authorities concluded in December 2003 that the debt situation was unsustainable and launched a debt exchange offer. The IMF has supported the authorities'

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

reforms since 2002 initially through a Stand-By Arrangement (SBA) and since end-2003 through a PRGF arrangement.

The reform strategy has been very successful. Economic growth has recovered to over 3 percent a year and is set to record the second straight year of above average growth in 2005. Inflation declined in 2004 and remains subdued in 2005 despite the higher energy prices. Reflecting strong fiscal consolidation and a collaborative debt restructuring agreement, public finances are now on a firmer footing. The central government primary balance has swung to a surplus of 4½ percent of GDP in 2004/05, with both higher revenues and lower spending contributing to the improvement. The debt restructuring process coupled with the fiscal consolidation effort allowed the debt stock to decline to 117 percent of GDP at end-2004. However, progress on structural reforms has been slower than expected, reflecting in part a limited implementation capacity and difficulties in building consensus.

Developments in the external position mirrors the economic recovery and the improved global environment. Import growth has been robust on account of the economic recovery but the impact on the current account has been partially offset by increased tourism receipts. Financial intermediation has also rebounded, and having contracted since early 2001, credit to the private sector has been growing from mid-2004. Private sector deposits grew moderately while net lending to government fell with the improved fiscal position, resulting in a substantial increase of the net foreign assets of commercial banks. Prudential indicators for the banking system's asset quality have remained broadly unchanged. However, poverty and unemployment remain serious concerns.

Executive Board Assessment

Executive Directors commended the Dominican authorities for the successful implementation of their economic program that has been supported by a PRGF arrangement since end-2003. Directors applauded the remarkable rebound in economic performance over the past two years, from the economic and financial crisis experienced in 2001−02. They attributed this turnaround to the strong policies being pursued by the authorities.

Directors pointed to the strong improvement in public finances, which has engendered confidence and restored the foundation for economic growth. Fiscal consolidation, which contributed to reversing the debt build-up, has helped reestablish macroeconomic stability. With the stability provided by the regional currency board arrangement and aided by the depreciation of the U.S. dollar in recent years, Directors considered that the competitiveness of the economy is adequate. Still, they stressed that Dominica continues to face significant challenges. They pointed in particular to the continuing very high level of debt, structural rigidities, and to the economy's large exposure to exogenous shocks, as evidenced by the recent rise in oil prices and the impact of preference erosion on the banana sector. Directors underscored the critical importance of policies to strengthen the resilience of the economy and sustain the growth momentum. They therefore called on the authorities to consolidate the gains thus far, with particular focus on fiscal discipline and consolidation and accelerated structural reforms.

Directors welcomed the recent steps to bolster public finances, but emphasized the need to reduce the debt burden further. They noted the adoption of value-added and excise tax legislation to allow for a VAT to come into effect on March 1, 2006, which should help improve the efficiency of the tax system. Directors welcomed the government's decision to publish information on tax concessions as an important step toward improving the transparency of public finances. They also noted the need for boosting the efficiency of government spending, streamlining public sector employment, and limiting the public sector investment program to well-targeted projects with high returns. In this regard, they welcomed the actions in the 2005/06 budget as further steps in the right direction. Directors also supported the government's objective of a smaller, more efficient, and better paid public service, but emphasized that this would require extensive rationalization of the structure and functions of ministries and departments. It will be important that the authorities continue targeting a primary surplus of 3 percent of GDP or higher, with a view to reducing debt to at least 60 percent of GDP over the next decade.

Directors commended the authorities for their efforts to reach collaborative agreements with creditors in the debt-restructuring process. They noted the depositing of payments to nonparticipating creditors into an escrow account as evidence of the authorities' good-faith approach. Directors were concerned, however, that reaching agreement with the last few hold-out creditors is taking time, and noted in particular the recent unfortunate actions by one large creditor. Directors recognized the importance of these creditors engaging with the authorities in a timely and constructive manner in order to reach a collaborative agreement. They also urged the authorities to complete expeditiously the issuance of the new bonds to participating creditors, and finalize the legislative changes needed to make these bonds tradable on the Eastern Caribbean Securities Exchange.

Directors emphasized the need for deepening structural reforms to sustain the current growth momentum. They welcomed the authorities' efforts towards removing bottlenecks that are impeding private investment. They noted the potential in the energy sector, and pointed to the benefits of liberalizing the electricity market to allow new entrants. Directors saw merit in rationalizing the operations of existing investment promotion agencies with a view to creating a one-stop investment promotion center. Directors also noted the need for modernizing the land registration process to ensure comprehensive coverage. Directors considered that, by creating a more enabling business environment, such reforms would do more, over time, to attract investment and stimulate private sector-led growth than the current reliance on tax incentives. In any event, it was considered that the region as a whole would be better served by a cooperative—rather than a competitive—solution to the tax incentive issue.

While noting that much progress had been made over the past two years, Directors pointed to the many challenges that persist in addressing vulnerabilities in the economy. They called for polices to prepare better for exogenous shocks, including those stemming from the high exposure to natural disasters. Directors also underscored the need to address the large unfunded liabilities of the social security system, which constitute a major risk to public finances. They stressed the importance of early and significant actions for social security reform, and were encouraged by the authorities' intention to review recommendations to overhaul the scheme. Directors also pointed to vulnerabilities in the financial sector, and the scope for strengthening regulatory oversight of nonbank institutions. They supported the provision of Fund technical assistance to strengthen the supervisory framework for AML/CFT in the nonbank sector, and encouraged the authorities to take the requisite actions. While the banking system remains generally sound, closer scrutiny of new bank lending was seen as helpful in reducing nonperforming loans. Directors noted that the manner in which these challenges are addressed will have a bearing on the durability of the economic recovery and sustainability of public finances.

Directors commended the authorities for seeking to bring the different elements of the reform agenda together in their forthcoming Growth and Social Protection Strategy document. They emphasized that progress in lowering unemployment and reducing poverty would depend critically on consolidating the gains made in macroeconomic stabilization and on fostering growth by creating a more conducive business environment. Directors noted that the present economic rebound and the government's renewed political mandate offer an important opportunity for the government to advance reforms. They called on the international community to support Dominica's reform effort, not least through speedy disbursement of already promised funds.

Directors encouraged the authorities to improve the quality of core statistics, which they considered key for effective surveillance.

Dominica: Selected Economic Indicators

	2002	2003	Prel. 2004	Proj. 2005
(Annual percentage change)				
Real sector				
Real GDP	-4.7	0.0	3.5	3.1
GDP deflator	-0.4	1.7	1.2	1.5
Consumer prices, end of year	0.4	2.9	0.8	1.5
(In percent of GDP)				
Public finances				
Central government overall balance 1/	-5.4	-1.3	-0.6	-2.5
Central government primary balance 1/	-1.6	5.6	4.4	3.0
Revenue and grants 1/	32.7	40.0	39.1	37.7
Expenditure and net lending 1/	38.2	41.3	39.6	40.2
Total public sector debt	127.2	130.6	116.7	109.1
(In percent of GDP, unless otherwise indicated)				
External sector				
Current account balance	-13.8	-13.0	-17.2	-19.2
Trade balance	-23.3	-27.4	-31.2	-33.0
Travel receipts	18.1	20.2	22.2	23.2
Exports, f.o.b. (percentage change)	-1.8	-6.0	3.0	5.2
Imports, f.o.b. (percentage change)	-11.5	9.3	13.5	8.6
Real effective exchange rate (percentage change) 2/	-6.3	-6.7	-7.0	...
External public sector debt (end of period)	79.9	84.4	81.2	81.1
(Annual percentage change)				
Money and credit				
Net foreign assets 3/	19.3	17.3	8.1	4.1
Net domestic assets 3/	-10.8	-16.4	-2.1	1.9
Private sector credit 3/	-1.3	-2.3	4.3	5.1
Broad money	8.5	1.0	5.9	6.0

Sources: Dominican authorities; Eastern Caribbean Central Bank; and IMF staff estimates.

1/ Data are on a fiscal year basis, beginning July 1 of the year shown.
2/ End of period (depreciation -).
3/ Changes relative to broad money at the beginning of the period.

INTERNATIONAL MONETARY FUND EXTERNAL RELATIONS DEPARTMENT

Press Release No. 05/227
FOR IMMEDIATE RELEASE
October 14, 2005

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Completes Fifth Review of Dominica's PRGF Arrangement, Approves US$1.7 Million Disbursement

The Executive Board of the International Monetary Fund (IMF) has completed the fifth review of Dominica's performance under its three-year Poverty Reduction and Growth Facility (PRGF) arrangement. The Board also completed Dominica's financial assurances review, which is required in accordance with the IMF Guidelines on Conditionality to ensure adequate safeguards of IMF resources, and approved a waiver for the non-observance of a continuous performance criterion on nonaccumulation of external payments arrears.

Additionally, the Executive Board approved a one-year extension of Dominica's repayment expectations to the IMF in a total amount equivalent to SDR 1.3 million (about US$1.8 million) arising from December 22, 2005 through December 22, 2006. The repayments will now fall due exactly one year after these dates.

As a result of the Executive Board's completion of the fifth review, Dominica can draw an amount equivalent to SDR 1.2 million (about US$1.7 million) under the PRGF arrangement, which will bring total disbursements to SDR 5.4 million (about US$7.7 million). The Executive Board approved Dominica's three-year PRGF arrangement on December 29, 2003 (see Press Release No. 03/228) for an amount equivalent to SDR 7.7 million (about US$11.1 million).

Following the Executive Board's discussion of Dominica on October 14, Mr. Agustín Carstens, Deputy Managing Director and Acting Chair, made the following statement:

"The Dominican economy has achieved a remarkable turnaround since the low-point of 2001–02, and is now set to record the second straight year of above average growth. The recovery is to a large extent a reflection of the authorities' successful implementation of their economic program and the resulting restoration of confidence. Continued progress with the reform agenda is essential to sustain the current momentum and address remaining vulnerabilities in the economy.

"The clearest evidence of the success of Dominica's adjustment program has been the marked strengthening of public finances. As a result, the public debt burden has been set on a downward course. Recent legislative changes will boost the efficiency of tax collection and increase the transparency of public finances.

"Public debt is still high, however, and fiscal policy will need to remain geared towards further debt reduction. The 2005/06 budget targets a primary surplus that appropriately balances the need to reduce debt with the need to reinstate the 5 percent cut in public wages introduced in the 2003/04 budget. Looking ahead, it will be important to continue targeting fiscal surpluses consistent with the objective of reducing debt to a more manageable level, including by a focused effort on containing the government's wage bill. Ideally, the aim should be to reduce the debt-to-GDP ratio to at least 60 percent over the next decade, which would provide an anchor for public expectations and improve the credibility of fiscal policy.

"Finalizing the debt-restructuring process will also help provide clarity to the debt issue. Dominica has made commendable progress in reaching collaborative agreements with most creditors, and continues to demonstrate good faith by depositing payments to nonparticipating creditors into escrow accounts under the restructured terms. It is a concern that agreements with the remaining nonparticipating creditors have not yet materialized. Although there appears to be progress in most cases, the recent actions by one outstanding creditor is unfortunate. As a result, continued efforts will be needed to reach a collaborative agreement and hence to complete the debt restructuring process in a timely fashion.

"A fundamental challenge going forward is to underpin the current growth momentum with further progress on structural reforms. Addressing remaining risks to public finances will be critical, including those from the large unfunded liabilities of the social security system. Removing bottlenecks that are impeding private investment should also be a high priority. This calls for reforming the electricity market to allow new entrants, rationalizing the existing investment promotion agencies, and modernizing the land registration process to ensure comprehensive coverage. Indeed, over time, such reforms to create a more enabling business environment are more likely to stimulate private sector led growth than the current reliance on tax incentives. Reducing financial sector vulnerabilities by strengthening regulatory oversight will also be important for maintaining macroeconomic stability.

"The Dominican authorities are seeking to bring all the different elements of the reform agenda together in their forthcoming Growth and Social Protection Strategy document. The premise is that progress in lowering unemployment and reducing poverty will depend critically on consolidating gains made in macroeconomic stabilization and on fostering a more conducive business environment. With the rebound in economic activity, the government is in a good position to carry out an ambitious reform agenda that will have a lasting impact on the economy. The international community, in turn, should actively support the authorities' efforts and objectives," Mr. Carstens said.