

**Annex to the Memorandum of Economic Policies of the Government
and Bank of Estonia**

Implementation of the economic program for 2000-2001 will be monitored through performance criteria and structural benchmarks.

I. Quantitative Performance Criteria

Overall General Government Balance

	Limit on Cumulative General Government Deficit (in EEK millions)
From January 1, 2000 to:	
March 31, 2000	410
June 30, 2000	700
September 30, 2000	750
December 31, 2000	1,000

General government operations encompass the budgets of the central government and local governments, including the foreign-financed expenditures of these institutions. The budget of the central government includes the state budget plus the Social Insurance and Medical Insurance Funds. The general government deficit is defined as total general government expenditures minus total general government revenues.

General government expenditures comprise all current and capital expenditures, including expenditures financed by foreign loans, and also include net lending by the general government.

General government revenues comprise all tax revenues plus non-tax revenues as reported by the Ministry of Finance. Receipts from the sale of state property in excess of EEK 10 million per object will not be included in non-tax revenues and will be regarded as a financing item.

Data on components of general government budget operations will be reported to the IMF within 30 days of the end of each month by the Ministry of Finance.

Net international reserves

		Minimum Level (in DM millions)
As of:	December 31, 1999	216
	January 1 through December 31, 2000	200

This floor will be adjusted:

- for any profit transfers to the state budget, and;
- by the amount of the proceeds from the sale of the Bank of Estonia's equity participation in Optivabank.

Net international reserves consist of gross foreign reserves of the Bank of Estonia, minus net liabilities of the Bank of Estonia (including currency board liabilities). The value of these assets and liabilities will be expressed in deutsche marks.

For the purposes of the program, the gross foreign reserves of the Bank of Estonia shall be defined as monetary gold, holdings of SDRs, any reserve position in the IMF, and holdings of foreign exchange in convertible currencies by the Bank of Estonia. Excluded from gross foreign reserves are capital subscriptions to foreign financial institutions, long term non-financial assets of the Bank of Estonia, and any assets in non-convertible currencies. Also excluded are assets held abroad by public enterprises and general government. On December 31, 1999, gross reserves of the Bank of Estonia, as defined here, amounted to EEK 13,334 million (equivalent to DM 1,667 million).

For the purposes of the program, **net liabilities of the Bank of Estonia** shall be defined as the Bank of Estonia's total liabilities, excluding Estonia's quota in the IMF and the Bank of Estonia's capital accounts. Government obligations associated with purchases under the STF will not be included among the net liabilities of the Bank of Estonia. On December 31, 1999, net liabilities of the Bank of Estonia, as defined here, amounted to EEK 11,604 million (equivalent to DM 1,450 million).

Performance will be monitored from information supplied monthly by the Bank of Estonia in the agreed format. The monthly data will be provided to the IMF within seven days of the end of each month throughout the program period.

Currency Board Cover

The Bank of Estonia will ensure that gross foreign reserves of the Bank of Estonia are at least equal to the currency board's liabilities at all times. Currency board liabilities will comprise kroon notes and coins in circulation, total reserve deposits of banks with the Bank of Estonia, certificates of deposit issued by the Bank of Estonia and kroon liabilities of the Bank of Estonia in its correspondent accounts. For the purposes of this performance criterion, currency board liabilities will be expressed in terms of foreign exchange using the official exchange rate of EEK 8 per deutsche mark. On December 31, 1999, currency board liabilities amounted to EEK 11,526 million (equivalent to DM 1,441 million).

Performance will be monitored from information supplied monthly by the Bank of Estonia in the agreed format. The monthly data will be provided to the IMF within seven days of the end of each month throughout the program period.

Ceilings on Contracting or Guaranteeing of New External Debt (In millions of U.S. dollars)

	Maturities		
	Two years and under	Over two years	Of which: over two years but less than ten years
Cumulative limits from January 1, 2000 to:			
March 31, 2000	0	130	(15)
June 30, 2000	0	200	(20)
September 30, 2000	0	250	(30)
December 31, 2000	0	250	(30)

During the program period, neither the government (including the central government), official extrabudgetary funds and entities, and local governments (but excluding the Bank of Estonia) shall contract or guarantee debt of an original maturity of two years or less, other than for normal import financing.

The government is defined in the same way as for the performance criterion for the overall balance of the general government. Excluded from the limits is the use of Fund resources; but other balance of payments support, including loans from official creditors and foreign banks, is included within these limits. The amount of debt contracted or guaranteed will be valued at the relevant currencies of denomination and converted into U.S. dollars using the Bank of Estonia's official exchange rates prevailing at the time the debt is contracted.

Observance of the limits shall be verified for the dates shown above. Information on contracting, guaranteeing and disbursements of external debt in the agreed format will be

reported monthly to the Fund within 30 days of the end of each month by the Ministry of Finance.

II. Structural Performance Criterion

The following will constitute a structural performance criterion under the program:

Basic Budget Law

The government will submit to parliament by June 30, 2000 a new draft Basic Budget Law that will, inter alia, provide for the inclusion in the government budget the utilization of foreign loans and grants and allow for greater control to be exercised over local authority budgets. The provisions of this Law would apply to the budget for 2001.

III. Structural Benchmarks

The main structural measures of the program will be monitored through structural benchmarks which are summarized in Table 2.

IV. Program Review

The first program review, to be concluded by June 30, 2000, will focus particularly on the evolution of the fiscal deficit and the implementation and adequacy of measures undertaken to contain this deficit within agreed limits. The second program review, to be concluded by December 15, 2000, will review the budget for 2001 and set program performance criteria for end-March and end-June 2001. This review will also focus on pension reform. The conclusion of both program reviews will be a performance criterion.

Table 1. Estonia: Quantitative Performance Criteria Under the 2000-2001 Program 1/

Performance Criteria			
(In millions of kroons)			
I. Limit on cumulative general government deficit:			
From January 1, 2000 to:			
March 31, 2000	410		
June 30, 2000	700		
September 30, 2000	750		
December 31, 2000	1,000		
(In millions of deutsche marks)			
II. Minimum levels for net international reserves of the Bank of Estonia 2/:			
December 31, 1999 (actual):	216		
January 1 through December 31, 2000	200		
III. Ceilings on external short-, medium-, and long-term debt of general government			
	Maturity of 0-2 years 3/	Maturity of over 2 years	of which: Maturity of more than 2 years but less than 10 years
(In millions of U.S. dollars)			
Cumulative changes from January 1, 2000 to:			
March 31, 2000	0	130	15
June 30, 2000	0	200	20
September 30, 2000	0	250	30
December 31, 2000	0	250	30
IV. The government will not accumulate external payments arrears during the period of the arrangement			
V. The currency board is to be fully backed with foreign exchange at all times 4/			

1/ Definitions of the concepts to be measured are set out in the Annex to the Memorandum of Economic Policies.

2/ This minimum level will be adjusted by any profit transfers to the state budget and by any proceeds from the sale of Optivabank.

3/ Excluding normal import financing.

4/ The gross foreign reserves of the Bank of Estonia did not fall below the currency board's liabilities through December 1999.

Table 2. Estonia: Structural Performance Criteria and Benchmarks
under the 2000-2001 Program

Measures	Implementation Date	MEP Paragraph
Structural Performance Criterion		
Submit new Basic Budget Law (including improved oversight and control over extrabudgetary funds, local governments, and agencies).	June 30, 2000	28
Structural Benchmarks		
1. Implement improved loan assessment framework, including a uniform minimum loan provisioning system in line with international standards.	March 31, 2000	33
2. Initiate assessment of compliance with good practice codes for fiscal and monetary policy.	June 30, 2000	20
3. Submit to parliament a new Securities Market Law in line with FSAP/FSSA recommendations..	June 30, 2000	34
4. Decide on organizational and legal principles for unified financial supervision agency	June 30, 2000	34
5. Complete upgrading of Energy Inspectorate	June 30, 2000	42
6. Submit to parliament complete pension reform package, including proposed eligibility criteria and benefits for second tier of pension system, consistent with World Bank/IMF recommendations.	December 1, 2000	39

Table 3. Estonia: Prior Actions under the Program

Measures	MEP Paragraph	Status
1. Finalize inspection manual to assist in the implementation of new internal regulations for consolidated supervision over banks.	31	Done
2. Implement revised bank disclosure requirements.	31	Done
3. Establish framework for transfer of Bank of Estonia profits to budget.	32	Done
4. Dispose of Hansabank shares held by Bank of Estonia.	36	Done
5. Halt transfers of privatization proceeds to Compensation Fund.	35	Done
6. Establish financial control departments within Ministry of Finance.	38	Done
7. Establish an Administrative Reform Bureau charged with reforming and streamlining central and local governments.	38	Done