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## **Republic of Palau: Recent Economic Developments**

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REPUBLIC OF PALAU

Recent Economic Developments

Prepared by Keon Lee, Torsten Sløk (both APD), and Curtis Hatch (TRE)

Approved by the Asia and Pacific Department

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## I. INTRODUCTION AND SUMMARY

1. **This paper provides a review of recent economic developments in Palau, covering the first five years of the Compact of Free Association (Compact) with the United States (1994/95–1998/99), as background for the staff report for the 1999 Article IV consultation.**

2. **Palau, an archipelago in the Western Pacific, has a small population of about 18,000, but a relatively high GDP per capita of over \$7,000 (Table 1).** Palau faces many development constraints common among Pacific island economies, including a narrow resource base, geographical isolation, a small domestic market, a lack of infrastructure and skilled labor, and vulnerability to external and natural shocks.

3. **The economy, comprising mainly services including a large public sector, grew rapidly in the first years of the Compact, as large Compact grants fueled consumption and investment, and tourist arrivals increased sharply (Table 2).** However, the economy entered a period of recession in 1998, as the Asian crisis brought about a marked downturn in tourism. Inflation appears to have been in the single-digit range in recent years, in line with inflation in the major partner countries (United States and Japan).

4. **Palau depends heavily on grants from the United States to finance otherwise unsustainable fiscal imbalances.** With a narrow tax base and high current expenditure (about half GDP in recent years), fundamental adjustments are required to adjust to the scheduled phasing down of U.S. grants during the next ten years (Compact grants are scheduled to end in 2008/09). The urgency of the situation has been increased by a marked deterioration of the fiscal position in 1998/99 (a budget deficit of 12 percent of GDP is expected for this fiscal year).

5. **After recording a large balance of payments surplus in 1994/95, reflecting up-front grant disbursements under the Compact, the balance of payments has been in deficit in three of the last four years.** Because of Palau's dependence on imports and its narrow export base, the trade account has experienced large deficits in recent years. However, the external current account (including grants) has continually been in surplus, owing to large tourist receipts, income from investing unspent Compact funds, and grants. The deficits in the overall balance of payments have reflected large capital outflows (recorded as errors and omissions), reflecting the pooling of deposits by large U.S.-based banks at their respective headquarters for investment elsewhere. As a result, Palau's foreign reserves (approximated by government financial assets, excluding the Trust Fund) have declined to around \$65 million in mid-1999 (equivalent to about a year of imports) from about \$100 million at end-1994/95 (Table 3).

6. **The banking system in Palau is generally in a good financial position, but has played a relatively limited role in promoting economic development.** The banks are not burdened by significant amounts of nonperforming loans (except the National Development

Bank of Palau), but this largely reflects the fact that the U.S.-based banks, which account for about 80 percent of deposits, place around two-thirds of their deposits at their headquarters abroad, while a large share of the local loans they do make is in the form of well-secured consumer loans rather than business loans. Increasing loan activity by these banks depends in particular on the clarification of land ownership and lease rights, as uncertainty in this area is preventing an effective use of land and leases as loan collateral. At the same time, there are currently no banking regulations covering locally chartered banks in Palau, which presents a potential systemic risk.

## II. OUTPUT AND PRICES

### A. Output

7. **Real GDP grew by 10–15 percent per annum during 1994/95–1995/96, reflecting the impact of large Compact grants on consumption and investment, and a sharp rise in tourist activity.** The sectors that experienced the fastest rates of growth were: wholesale and retail trade, and transportation, to handle increasing volumes of imports; hotels and restaurants, to accommodate the growing numbers of tourists;<sup>1</sup> and construction, reflecting a five-fold increase in government spending on infrastructure during 1994/95–1995/96 (Table 2).

8. **However, real GDP growth stalled in 1996/97 and subsequently turned negative in 1997/98, owing to the impact of the Asian crisis on tourism and the phasing down of U.S. grants under the Compact.** Real GDP is now expected to decline by about 5 percent in 1998/99, after falling by a similar amount in 1997/98. Tourists from the region were discouraged by the downturn in their economies, as well as the considerable appreciation of the U.S. dollar against their currencies (the U.S. dollar is legal tender in Palau). As a result, the hotels and restaurants, and trade sectors contracted sharply in 1996/97–1997/98. With the phasedown of grants, the government kept a tighter hold on current expenditure and cutback on capital spending, which dampened growth in the construction and public sectors in the last few years.

9. **The greatest potential for future growth clearly lies in tourism.** Tourist activity in Palau currently is limited to scuba diving and snorkeling, but there is potential to also provide facilities for golfing, hiking, and biking, particularly with the development of Babeldaob, the largest island. The construction of a ring road around Babeldaob, which is scheduled to begin in late 1999, should greatly improve access. Fisheries, a traditionally important sector consisting primarily of commercial fishing in Palau's exclusive economic zone, is likely to

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<sup>1</sup>Tourists from Taiwan, Province of China increased sharply, with the opening of a chartered flight in 1995. At the same time, the average expenditure per tourist is estimated to have increased from \$882 in 1994 to \$937 in 1997.

continue to decline owing to oceanographic changes (this sector has also been adversely affected by falling prices of high-grade tuna and reduced demand owing to the Asian crisis). Agriculture (mostly subsistence) accounts for only 2 percent of GDP, and manufacturing is small, consisting mainly of a small number of establishments involved in bakeries, garments, building materials, furniture, and handicrafts.

## **B. Prices, Wages, and Employment**

10. **Inflation in Palau, based on anecdotal evidence, has been in the single-digit range in recent years**, in line with inflation in neighboring Guam and Saipan, and its major trading partners (Japan and the United States).<sup>2</sup> In addition to the U.S. dollar providing an anchor for prices, there are indications that the current economic slowdown has had a dampening effect on wages: the average gross wage for the economy (as reported by the social security administration) increased by 6.3 percent in 1997 and 0.5 percent in 1998, while the average gross government wage rose by 7.7 percent in 1997 and fell by 1 percent in 1998.

11. **Employment has been growing steadily over the last five years** reflecting mainly the steady inflow of workers mostly from the Philippines (the native Palauan population has grown only very slowly in recent years).<sup>3</sup> Many Palauans tend to work in the public sector, where wages on average have been about double the wages in the private sector, while the non-Palauans tend to work in tourism-related service sectors. The public sector remains the largest employer, accounting for about one-third of total employment in recent years (Table 4).

## **III. PUBLIC FINANCES**

### **A. Overall Developments**

12. **The public sector is made up of the national government, 16 state governments, and nonfinancial public enterprises.** The national government conducts budgetary operations through four main funds: (1) the general fund; (2) the special fund; (3) the capital project fund; and (4) the debt-service fund. Transfers are made between these funds, mainly from the general fund to other funds within the national government, but from the general fund to the state governments' funds as well. There is, however, very limited or no authority for the use of foreign grants earmarked for capital projects to finance current expenditures.

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<sup>2</sup>Consumer price data are not compiled in Palau. The government is currently in the process of gathering price data with UNDP assistance, and a consumer price index is expected to be available in 2000. There are also no reliable time-series data on wages, except for the census survey carried out every five years (the last one was in 1995).

<sup>3</sup>Based on 1995 census data, about 40 percent of the total employed were born outside Palau, of which about two-thirds were from the Philippines.

13. **The budget recorded a surplus of about \$100 million (100 percent of GDP) in 1994/95, reflecting very large upfront grant disbursements under the Compact (\$143 million)<sup>4</sup> (Tables 5 and 6).** While grants fell sharply in the following year, as scheduled, to about \$35 million, current and capital spending accelerated with the greater availability of funds, giving rise to a budget deficit of 8 percent of GDP. The budget returned to a surplus in 1996/97–1997/98, but mainly because of one-time revenue gains (unusually high earnings on investments in U.S. stocks in 1996/97 and a large legal settlement pertaining to the collapse of a bridge in 1997/98). In 1998/99, the fiscal position is expected to worsen sharply, reflecting in addition weak tax revenues stemming from the recession, a scheduled step-down in Compact grants, and an acceleration of current spending.

### **B. Revenue and Grants**

14. **Reflecting a narrow base and problems in administration, tax revenue has remained relatively low in relation to GDP (Table 5).** Tax revenue comes mainly from a 4 percent gross receipts tax on business (after allowable deductions for wages and salaries paid to workers), income tax on wages and salaries, the import tax, and tourism-related taxes (mainly hotel occupancy and airport taxes).<sup>5</sup> Tax revenue has remained low despite a number of changes in recent years: (1) starting in 1995/96, the government reduced the share of wages paid to noncitizen workers deductible for gross receipts tax purposes from 100 percent to 50 percent; (2) “sin taxes” on imports of cigarettes and tobacco products, and on liquors and other beverages were raised in 1996 and again in 1998; (3) exemptions from taxes for commercial imports were eliminated in 1994, while the exemptions for personal imports were removed in 1998, leaving only government imports still exempt from taxes; and (4) the airport tax has been raised in stages to \$20 per head from \$5 for citizens and \$10 for noncitizens prior to the Compact.

15. **Since 1994/95, nontax revenue has been dominated by earnings from the investment of unspent Compact grants.** Excluding income from the Compact Trust Fund (which is essentially escrowed for future use and is therefore treated separately from normal budget operations), investment income has fluctuated within a range of \$5–8 million a year consistent with the strong performance of the U.S. stock market.<sup>6</sup> Fees and charges have also been a major source of nontax revenue, while fishing rights fees have been declining with the

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<sup>4</sup>The total amount included \$17 million of non-Compact grants, mostly from the United States, but excluded a disbursement of \$66 million into the Compact Trust Fund in 1994/95.

<sup>5</sup>There are no taxes on investment income. See Table 5a for a summary of Palau’s tax system.

<sup>6</sup>In 1996/97, a further \$3 million was raised from the government selling its holdings in Continental Micronesia.

fishing industry. In 1997/98, nontax revenue was boosted by a \$13 million legal settlement pertaining to the collapse of the Koror-Babeldaob bridge.

16. **However, grants remain the largest source of government receipts.** U.S. grants account for almost all foreign aid and are mainly provided under the Compact or by the U.S. Department of Interior (Table 6). However, both Compact and non-Compact U.S. grants are scheduled to be phased out over time. Grants under the Compact, after a peak of \$126 million (excluding the Trust Fund) in 1994/95, will be phased down from above \$20 million per annum during 1995/96–1997/98 to around \$14–15 million a year during 1998/99–2008/09. There are no commitments for grants under the Compact beyond 2008/09.

### C. Expenditure

17. **Current expenditure has remained high, though it has declined from well above 50 percent of GDP in 1994/95 to around 45 percent of GDP in the last few years.** About 90 percent of total current spending has been accounted for by wages and salaries (fueling the growth of public sector employment and supporting relatively high public sector wages), and purchases of goods and services (Tables 5 and 7). Subsidies to public enterprises, after reaching nearly \$8 million in 1995/96, have declined sharply to an estimated \$1.4 million in 1998/99, as large subsidies provided to the Public Utilities Corporation (PUC) were eliminated in 1998/99.<sup>7</sup>

18. **Capital expenditure, which focuses on the physical infrastructure, has fallen to about 8 percent of GDP in the last two years from some 14 percent of GDP in 1995/96–1996/97.** Non-Compact capital expenditures have declined from about \$6 million in 1994/95–1995/96 to less than \$2 million in 1997/98, as existing pre-Compact projects near completion. Capital expenditure using Compact grants earmarked for capital improvement<sup>8</sup> rose sharply from less than \$3 million in 1994/95 to \$10 million in 1995/96 and \$13 million the following year, as many of the projects held back pending the signing of the Compact came on stream. After the initial spurt, however, capital spending has slowed considerably (\$7.6 million in 1997/98).

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<sup>7</sup>In 1995/96, PUC accounted for \$7 million of the \$7.9 million of total subsidies to public enterprises, with the Palau Visitors' Authority (PVA) accounting for another \$0.7 million (reflecting the government's efforts to promote tourism in Palau). In 1998/99, no subsidies were budgeted for PUC, and most of the \$1.4 million of subsidies to public enterprises is estimated to be received by the PVA.

<sup>8</sup>Under Section 212(b) of the Compact, \$52 million (including inflation adjustment) was disbursed in 1994/95 for infrastructural projects.



#### D. Local Governments

19. **The main sources of local government revenue are national government grants, fishing rights fees, and other local fees and charges, such as motor vehicle registration fees and payments for business and import licenses.** Local government expenditures typically cover local wages and salaries, municipal and civic services, and small-scale capital expenditures (Table 8). The authorities indicated that local governments were under strict instructions to keep spending within available resources, that is, local revenues plus grants from the national government.

#### E. Trust Funds

20. **There are three trust funds administered by the government: the Compact Trust Fund, the Social Security Fund, and the Civil Service Pension Fund.** Two disbursements were made under the Compact for investment in the Compact Section 211(f) Trust Fund (\$66 million in 1994/95 and \$4 million in 1996/97), the future proceeds of which can be used only after the annual Compact grants end in 2008/09 (see Annex II of the staff report for more details). The government has been investing these funds in a U.S. securities portfolio managed by U.S. investment managers. The market value of the Compact Trust Fund holdings amounted to \$141 million at end-May 1999, about 13 percent higher than envisaged under the Compact at this time (Table 9).

21. **Palau's social security system is self-financing by law (the government only provides employers' contributions), and provides retirement, disability, and death benefits to qualified individuals and their surviving families.** All employees of the public and private sectors are covered under the system. Presently, there are over 29,400 active and inactive members of the system, with approximately 1,300 members and surviving spouses and children receiving social security benefits. With a sizable balance in the Social Security Fund (\$23 million at end-1997/98), and revenues still much larger than expenditures (Table 10), the social security system will be able to continue to meet its current obligations for some time, although, based on the latest actuarial valuation, the system is underfunded by \$19 million.

22. **The Civil Service Pension Fund provides retirement, disability, death, security, and other benefits to civil servants, and their spouses and dependents.** The government has made a number of contributions to the Pension Fund recently (Table 11). Total revenues have exceeded expenditures, and the total Pension Fund balance at end-1997/98 amounted to \$22.4 million. The government recently changed the mandatory retirement age from 60 years to 30 years' service (effective July 1, 1999). While the Pension Fund is able to meet its current payments, it is estimated to be underfunded (on an actuarial basis) by \$23 million.

## F. Nonfinancial Public Enterprises

23. **Four nonfinancial public enterprises have received budgetary subsidies in recent years:** PUC, PVA, the Belau National Museum, and the Palau Housing Authority (see Annex VI of the membership paper, EB/CM/Republic of Palau/97/1 (7/25/97), for a description of the institutional and operational aspects of these enterprises and other public entities). In the absence of large subsidies, the PUC made substantial losses in 1996/97–1997/98 and is expected to make further losses in 1998/99 (Table 12). Subsidies to PVA have increased considerably in recent years, reflecting the government's strong intention to promote tourism in Palau. The Palau Housing Authority receives a small subsidy annually to provide low-cost housing for Palauan families (Table 13). It recorded small surpluses in the latest three years for which data are available (1994/95–1996/97). The Palau National Communication Corporation has not received subsidies in recent years, but made a loss in 1997/98 for the first time since the early 1990s, as the Asian crisis adversely affected tourism and thus significantly reduced the volume of international phone calls (Table 14).

## IV. MONEY AND BANKING

24. **Palau uses the U.S. dollar as legal tender and has no central bank.** Palau's financial sector consists of eight commercial banks and one development bank, the National Development Bank of Palau (NDBP). The largest three commercial banks (Bank of Hawaii, Bank of Guam, and Guam Savings and Loans) are U.S.-based and account for more than 80 percent of total deposits. The other five are smaller locally chartered banks (Bank of Palau, Pacific Savings Bank, Bank of Micronesia, Palau Construction Bank, and Melekeok Government Bank). In states other than the capital of Koror, there are some very small credit unions serving local banking needs.

25. **A monetary survey is not available in Palau,** as the banks do not provide balance sheet data to the authorities. However, the three largest U.S.-based banks had deposits in total of about \$85 million as of mid-1999, of which only about \$30 million were loaned out in Palau. Most of the remainder is pooled in their respective headquarters for investment elsewhere. Clearly, significant amounts of financial capital (private and government savings) are being exported from Palau via the banking system. About one-half of the domestic loans are small consumer loans, typically serviced by withholding from borrowers depositing their salaries in these banks. The consumer loans are thereby well secured and the banks reported minimal defaults on these loans. However, the banks tend to be wary of expanding their business lending operations, as they view this type of lending to carry considerable credit risk in Palau, especially for business startups. While there are ceilings on interest rates on loans in Palau,<sup>9</sup> the banks view as a more serious problem the fact that foreigners (and foreign-owned

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<sup>9</sup>18 percent per annum for loans under \$15,000 (mainly consumer loans); and the U.S. prime rate plus 4 percentage points for loans greater than \$15,000 (see Tables 15 and 16 for selected actual interest rates).

banks) cannot own land under Palauan law and that there is a great deal of uncertainty about rights to land leases, which makes it very difficult to use land or leases as loan collateral.

26. **The NDBP<sup>10</sup> provided a solution to this problem to some extent as it would guarantee 90 percent of business loans for a fee** (the NDBP would take possession of the land in case of default). However, the NDBP has been unable to provide such guarantees in the last couple of years, as its own balance sheets had deteriorated significantly. Some 30 percent of the NDBP's loan portfolio is currently nonperforming, owing partly to poor loan assessment skills, but also to a lack of accountability for the management of the bank. Consequently, the NDBP has been in a consolidation mode for the past couple of years in an attempt to solidify its balance sheet prior to resuming its lending and guaranteeing operations (Tables 17–19).

27. **Although banks in Palau are licensed by the Attorney General's Office, there are currently no banking regulations in Palau.** The deposits of Palau branches of U.S.-based banks are insured by the FDIC and these banks are required to follow U.S. banking regulations. The local banks tend to follow some of these regulations in order to have a corresponding relationship with a U.S. bank, but banking regulations have yet to be formulated. There are presently no serious concerns about the health of the banks (except the NDBP, which cannot by law accept deposits), as nonperforming loans are small, reflecting banks' preference for consumer loans.

## V. EXTERNAL SECTOR

### A. Current Account

28. **The current account deficit excluding grants narrowed from 15 percent of GDP in 1994/95–1995/96 to 6 percent of GDP in 1996/97, reflecting strong growth of tourism earnings and a spike in investment earnings in 1996/97** (Table 20). However, the deficit has subsequently widened to around 10 percent of GDP in the last two years, owing to the adverse impact of the Asian crisis on tourism earnings and a return of investment earnings to more normal levels, although the deterioration has been partly offset by lower trade deficits reflecting the import compression. The current account including grants has been further exacerbated by the step-down in Compact grants in 1998/99 by the equivalent of 4½ percent of GDP.

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<sup>10</sup>The NDBP receives the bulk of its resources from government transfers and U.S. grants. Its main objective is to provide low-cost capital for projects with development potential in the private sector.

## **Merchandise trade**

29. **Palau's exports, consisting almost exclusively of fish (sashimi-grade tuna headed for Japan), have fallen in recent years;** total exports amounted to 9 percent of GDP in the last two years, compared with 12 percent of GDP in 1995/96. The decline in fish exports reflected an overall decline in fish catch, a weakening in export prices from 1996 onward, and lower levels of demand following the onset of the Asian crisis. In addition, the fishing industry has been hampered by limited air freight capacity, due to infrequent commercial and charter flights out of Palau.<sup>11</sup> Other exports consist mostly of garments and handicraft.

30. **Imports rose rapidly during 1994/95–1996/97, reflecting growing consumption and investment fueled by U.S. grants and rising demand from the tourism industry,** although its size relative to GDP remained relatively constant at somewhat above 50 percent of GDP. However, imports have since declined with the recession. Imports consisted primarily of fuel, food and beverages, machinery and equipment, and miscellaneous manufactured articles (Table 21). The United States (including Guam) was by far the largest source of imports, followed by Japan and Singapore (Table 22).

## **Services, income, and transfers**

31. **Services account receipts are mostly made up of earnings from tourism,** which more than doubled to over \$60 million (47 percent of GDP) between 1993/94 and 1996/97. This reflected a doubling of tourists to 66,000, mostly accounted for by increases in visitors from Taiwan, Province of China (Table 23). However, tourists proved to be highly sensitive to the Asian crisis and their numbers fell both because of the relative appreciation of the U.S. dollar and because of declining incomes.<sup>12</sup>

32. **Service account payments comprise mostly freight and insurance costs,** estimated at about 25 percent of the f.o.b. value of imports. The relatively high figure reflects Palau's remote location and reliance on air transportation, and is in line with estimates for the neighboring island economies.

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<sup>11</sup>The fishing fleet based in Palau has been halved in the last five years to less than 150 vessels in 1998.

<sup>12</sup>Weighted by shares in tourist arrivals, Palau's nominal effective exchange rate appreciated by 21 percent during June 1997–June 1998, though about half of this appreciation has since been reversed. The Taiwanese dollar depreciated by about 20 percent against the U.S. dollar during June 1997–June 1998 and by 14 percent during June 1997–May 1999. With inflation in Palau likely to be in line with the low inflation in the major partner countries, the appreciation in the real effective exchange rate is probably in a similar range.

33. **Sizable income has been generated from the investment of Compact grants (excluding the Trust Fund), and the Social Security and Civil Service Pension Funds.** Investment income hit a peak of \$18 million (14 percent of GDP) in 1996/97, but has since declined to around \$7 million in the last couple of years, partly reflecting the drawdown of government financial assets.

34. **Both inflows and outflows of private transfers (remittances) have increased steadily in recent years.** Remittances by Palauans working abroad (mostly in Guam, Saipan, and Hawaii) rose to over \$1 million in the last few years, while outward remittances (mainly by Filipino workers in Palau) have also risen to more than \$7 million, reflecting a significant rise in the number of foreign workers.

35. **Official current grants peaked at \$85 million in 1994/95, reflecting frontloaded Compact disbursements,** then dropped to around \$30 million a year during 1995/96–1997/98, and subsequently to \$22 million in 1998/99. Fishing rights fees, collected mainly from distant water fishing vessels from Japan, have remained relatively unchanged at around \$1 million in recent years.

#### **B. Capital Account and External Debt**

36. **Data on capital account transactions are scarce, partly owing to a lack of commercial banking statistics.** Official capital grants, earmarked for infrastructural investment, rose sharply to \$62 million in the first Compact year (1994/95), but has since dropped off to \$2–3 million a year more recently. There has, however, been an increase in capital grants from Japan for utilities improvement and fisheries development, albeit from a low level.

37. **Palau has modest external debt of about \$5 million as of mid-1999,** arising from the financing of a power plant. The original debt of \$60 million incurred for the power plant was renegotiated in 1994 to an interest-free debt of \$20 million, with a stream of repayments of around \$4 million a year for five years starting in 1995. The debt is expected to be fully repaid in 1999/2000 (Table 24).

38. **There are no official data on foreign direct investment,** but a number of private investments (mainly in hotels, fisheries, and a garment factory) have been financed in recent years through joint ventures with foreign private capital.

39. **Large negative errors and omissions suggest that there has been significant outflows of private capital in recent years** (Table 20), reflecting the pooling of resources by banks noted earlier. A sharp decline in errors and omissions in 1997/98 likely reflects that many banks faced increased deposit withdrawals in the summer of 1998, as many businesses and consumers were squeezed for cash as the Asian crisis intensified.

### C. Exchange and Trade System

40. **The currency of Palau is the U.S. dollar.** The authorities do not transact in foreign exchange. Most commercial banks handle foreign exchange transactions and buy and sell foreign currencies on the basis of rates quoted in the international markets. There are no taxes or subsidies imposed on the purchase or sale of foreign exchange. The Republic of Palau accepted the obligations of Article VIII, Sections 2, 3, and 4 on December 16, 1997.

41. **Imports are not subject to any licensing requirements,** but importers must obtain a business license to engage in importing activities. Specific and ad valorem taxes are levied under the Customs Rules and Regulations. Specific duties are levied on cigarettes, alcoholic products, and other beverages. Ad valorem duties are assessed on other products (using f.o.b. values) ranging from 3 percent (most products) to 150 percent (tobacco products other than cigarettes).

42. **There are no surrender requirements for export proceeds.** Exports are not subject to licensing requirements, except with regard to the export of fish. There are no taxes or quantitative restrictions on exports, except that, under the Fish Export Tax Law, as amended, a tax is levied on the export of any species of tuna and any species of billfish at the rate of \$0.25 per kilogram.

43. **There are no restrictions on the payments for or receipts from invisibles.**

44. **Foreign investors are required to submit applications to the Foreign Investment Board and obtain an approval certificate to engage in business or to acquire an ownership interest in a business in Palau.** Some business activities are reserved exclusively for Palauan citizens or business enterprises wholly owned by Palauan citizens; these include wholesale or retail trade in goods, land transportation, and some tourism and travel activities. There are no special financial incentives offered to foreign investors, except those available under certain provisions of the Compact (for example, duty-free access to the U.S. markets for some products). Foreign ownership of real estate is prohibited, but foreigners can obtain long-term leases extending up to 50 years. There are no restrictions on the repatriation of profit or capital.

Table 1. Republic of Palau: Selected Social Indicators

GDP per capita (U.S. dollars, 1998)	7,137
Area (square miles)	
Land	188
Sea	237,850
Demographic indicators (1995)	
Total population	17,225
Population growth (percent per annum)	
1986-90	2.4
1990-95	2.6
Crude birth rate (per 1,000)	23
Crude death rate (per 1,000)	6
Infant mortality (per 1,000)	18
Labor force	8,343
Employed	7,759
Agriculture, fisheries, and mining	724
Construction	1,087
Manufacturing	78
Transport, storage, communication, and other public utilities	435
Wholesale, retail, restaurants, and hotels	1,448
Finance, insurance, and real estate	122
Other business, personal, community, and social services	1,573
Public administration	2,292
Unemployed	584
Age structure (in percent)	
0-14	28.1
15-64	66.2
65 and over	5.7
Public health and education (1990)	
Education	
Percent graduating	
Primary	98
Secondary	58
Student/teacher ratio	11
Health	
Number of inhabitants per dispensary	1,325

Sources: *Palau Statistical Yearbooks 1998 and 1999, 1995 Census of Population and Housing, National Master Development Plan.*

Table 2. Republic of Palau: Gross Domestic Product, 1992-98

	1992 1/	1993 1/	1994 2/	1995 2/	1996 3/	1997 3/	1998 Est.
(In thousands of U.S. dollars)							
Agriculture	2,210	2,273	2,346	2,420	2,493	2,450	2,650
Fisheries	13,063	5,809	4,967	4,124	3,282	3,520	3,485
Mining and quarrying	528	587	444	301	158	138	145
Manufacturing	592	560	740	921	1,102	968	1,016
Electricity, gas, and water	855	923	608	294	-20	-502	-427
Construction	8,394	4,535	4,869	7,903	9,258	10,006	10,006
Trade	14,014	14,044	14,751	20,388	24,559	22,597	20,337
Hotels and restaurants	5,451	6,418	7,132	13,610	16,504	16,476	14,334
Transport and communication	9,313	9,980	10,476	14,429	17,355	19,855	20,649
Finance and insurance	2,404	2,044	3,245	4,446	5,647	6,573	7,231
Real estate and business services	3,233	3,646	4,118	4,589	5,061	7,791	8,571
Public administration	18,439	20,442	22,989	23,203	26,904	29,319	28,879
Other services	2,859	2,970	5,875	6,119	9,104	9,354	9,214
Subtotal	81,356	74,230	82,560	102,747	121,405	128,546	126,091
Less: Imputed bank service charge	1,256	1,029	1,011	993	975	1,250	1,250
Plus: Import duties	2,351	2,707	3,082	3,457	3,832	3,842	4,410
Gross domestic product	82,451	75,907	84,630	105,211	124,262	131,138	129,251
(In percent of total)							
Agriculture	2.7	3.0	2.8	2.3	2.0	1.9	2.1
Fisheries	15.8	7.7	5.9	3.9	2.6	2.7	2.7
Mining and quarrying 3/	0.6	0.8	0.5	0.3	0.1	0.1	0.1
Manufacturing	0.7	0.7	0.9	0.9	0.9	0.7	0.8
Electricity, gas, and water	1.0	1.2	0.7	0.3	0.0	-0.4	-0.3
Construction	10.2	6.0	5.8	7.5	7.5	7.6	7.7
Trade	17.0	18.5	17.4	19.4	19.8	17.2	15.7
Hotels and restaurants	6.6	8.5	8.4	12.9	13.3	12.6	11.1
Transport and communication	11.3	13.1	12.4	13.7	14.0	15.1	16.0
Finance and insurance	2.9	2.7	3.8	4.2	4.5	5.0	5.6
Real estate and business services	3.9	4.8	4.9	4.4	4.1	5.9	6.6
Public administration	22.4	26.9	27.2	22.1	21.7	22.4	22.3
Other services	3.5	3.9	6.9	5.8	7.3	7.1	7.1
Subtotal	98.7	97.8	97.6	97.7	97.7	98.0	97.6
Less: Imputed bank service charge	1.5	1.4	1.2	0.9	0.8	1.0	1.0
Plus: Import duties	2.9	3.6	3.6	3.3	3.1	2.9	3.4
Gross domestic product	100.0	100.0	100.0	100.0	100.0	100.0	100.0
(In percent)							
Memorandum items:							
Nominal GDP growth	-1.7	-7.9	11.5	24.3	18.1	5.5	-1.4
Real GDP growth 4/	-6.4	-12.3	5.6	14.8	7.8	0.7	-5.2

Source: Data provided by the Palauan authorities; and Fund staff estimates.

1/ Data for 1992 and 1993 are from the University of Oregon and the U.S. Department of the Interior.

2/ Data for 1994 and 1995 have been estimated using indicators for tourism, trade, and public administration between 1993 and 1996 benchmarks.

3/ Data for 1996 and 1997 have been estimated by a UNDP statistics specialist.

4/ Inflation data are not available for Palau. Nominal GDP is deflated by inflation in the neighboring Marshall Islands as an approximation.



Table 3. Republic of Palau: Financial Holdings of the Central Government, 1992/93-1997/98

(In thousands of U.S. dollars; end of period)

	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98
Foreign assets 1/ Deposits with foreign banks	...	...	95,688	81,793	76,296	67,527
Domestic assets 2/ Deposits with domestic banks	854	474	622	2,300	4,715	17,580
Fiduciary funds 3/	...	...	70,779	77,176	105,536	122,362
Total financial holdings	854	474	168,250	161,269	186,547	207,469

Source: Data provided by the Palauan authorities.

1/ Deposits with all foreign banks, including those in the United States.

2/ Deposits with local banks.

3/ Refer only to Compact Section 211(f) Trust Fund, excluding the Civil Service Pension Trust and Social Security Retirement Fund.

Table 4. Republic of Palau: Employed Persons by Industry, 1990 and 1995

	1990 Census	1995 Census
Agriculture, fisheries, and mining	446	724
Construction	861	1,087
Manufacturing	93	78
Transport, storage, communication, and other public utilities	477	435
Wholesale, retail, restaurants, and hotels	800	1,448
Finance, insurance, and real estate	119	122
Services 1/	687	1,573
Public administration	2,116	2,292
Total employed population	5,599	7,759

Sources: Office of Planning and Statistics, *1994 Statistical Yearbook*; *1995 Census of Population and Housing*.

1/ Includes business, repair, personal, entertainment and recreation, health, education, and social services.

Table 5. Republic of Palau: National Government Budgetary Operations, 1992/93-1998/99

	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98	1998/99 Budget
(In thousands of U.S. dollars)							
Total revenue and grants	49,407	49,619	166,176	65,960	72,270	73,366	57,730
Domestic revenue	18,023	18,762	23,159	28,509	39,098	43,385	33,412
Tax revenue	11,269	12,712	13,351	15,637	16,829	19,037	20,964
Salaries and wages	3,060	3,455	3,822	4,096	4,620	4,720	5,307
Import tax	2,707	3,258	3,136	3,298	3,850	4,410	5,311
Gross revenue tax	4,194	4,753	4,774	6,068	6,260	6,260	6,749
Other	1,308	1,246	1,619	2,175	2,099	3,647	3,597
Nontax revenue	6,754	6,050	9,808	12,872	22,269	24,348	12,448
Fishing rights income	224	198	230	210	130	120	125
Fees and charges	3,394	3,824	1,247	1,195	1,158	1,440	732
Other	2,696	1,549	1,043	1,713	2,088	15,288	2,885
Local trust funds	441	479	1,082	1,574	1,786	2,696	2,116
Investment income	...	...	6,206	8,180	17,107	4,804	6,590
Compact	...	...	6,206	8,180	14,055	4,804	6,590
Other	...	...	...	...	3,052	0	0
Grants	31,384	30,857	143,017	37,451	33,172	29,981	24,318
Compact	...	...	126,467	23,522	22,356	21,220	13,762
Other 1/	31,384	30,857	16,550	13,929	10,816	8,761	10,556
DOI grants for operation	18,054	18,091	207	541	374	588	1,500
DOI grants for CIP	3,792	3,012	4,733	5,139	2,782	1,297	1,300
Non-DOI capital projects	...	...	1,081	1,252	792	249	949
Grants from U.S. grantor agencies	9,538	9,755	10,224	6,698	6,638	6,038	6,009
Other countries grants	...	...	305	299	230	589	798
Total expenditure	46,576	50,383	65,251	75,148	76,542	64,617	80,842
Current expenditure	42,785	47,371	56,722	58,145	58,252	54,761	63,738
Wages and salaries	20,442	22,989	23,203	25,820	27,777	27,355	29,248
Purchases of goods and services	21,985	21,958	23,627	19,896	25,298	22,982	26,410
Interest payments	0	0	83	0	0	0	0
Subsidies and other current transfers 2/	357	2,424	9,809	12,429	5,177	4,424	8,080
Public enterprises	207	266	5,543	7,889	3,037	1,964	1,350
Other	150	2,158	4,266	4,540	2,140	2,460	6,730
Capital expenditure	3,792	3,012	8,529	17,003	18,290	9,856	17,104
Errors and omissions, accounts payable/receivables	-2,592	1,143	-115	-29	4,590	-1,053	0
Overall balance	239	380	100,810	-9,217	318	7,696	-23,112
Financing	239	380	-100,810	9,217	-318	-7,696	23,112
Net long-term borrowing	0	0	-4,500	-3,000	-3,400	-3,600	-4,067
New borrowing	0	0	0	0	0	0	0
Principal repayments	0	0	4,500	3,000	3,400	3,600	4,067
Other (-) equal increasing assets 3/	239	380	-96,310	12,217	3,082	-4,096	27,179
(As a percent of fiscal year GDP)							
Total revenue and grants	63.4	60.2	166.1	55.2	55.8	56.6	...
Domestic revenue	23.1	22.8	23.1	23.9	30.2	33.4	...
Tax revenue	14.5	15.4	13.3	13.1	13.0	14.7	...
Nontax revenue	8.7	7.3	9.8	10.8	17.2	18.8	...
Of which : Investment income 4/	0.0	0.0	7.3	8.2	14.6	5.8	...
Grants	40.3	37.4	142.9	31.3	25.6	23.1	...
Total expenditure	59.8	61.1	65.2	62.9	59.1	49.8	...
Current expenditure	54.9	57.5	56.7	48.7	45.0	42.2	...
Capital expenditure	4.9	3.7	8.5	14.2	14.1	7.6	...
Overall balance	0.3	0.5	100.7	-7.7	0.2	5.9	...
Overall balance, excluding grants	-39.9	-37.0	-42.2	-39.1	-25.4	-17.2	...
Memorandum items:							
GDP (calendar year)	75,907	84,630	105,211	124,262	131,138	129,251	...
GDP (fiscal year) 5/	77,894	82,450	100,066	119,500	129,419	129,723	...

Sources: Reports on the Audit of Financial Statements for fiscal years 1992/93-1997/98 (data for 1998/99 are preliminary); and data provided by the Palauan authorities. Fiscal year runs from October to September.

1/ Includes mainly grants from U.S. Department of Interior (DOI) and other U.S. agencies. These grants are used to support both current and capital expenditures.

2/ Includes subsidies and transfers for current operations.

3/ Excluding trust fund.

4/ Includes local trust funds and investment income.

5/ Calculated using simple quarterly interpolation.

Table 5a. Republic of Palau: Summary of Tax Structure, 1998/99

Type of Tax	Nature of Tax	Exemptions and Deductions	Rate Structure
Wages and salaries tax.	<p>The wages and salaries tax is payable on the gross income from wages and salaries of all individuals who work in the Republic of Palau. This includes Palauans, U.S. citizens, and other expatriates who work under contracts.</p> <p>The wages and salaries tax is payable to the National Treasury within 30 days after making disbursement of wages and salaries to the employee.</p> <p>This is applicable to all citizens and noncitizens. U.S. embassy personnel are not subject to the tax.</p>	<p>There is an annual exemption of \$2,000.</p>	<p>6 percent (\$0-\$8,000). 12 percent over \$8,000.</p>
Gross revenue tax.	<p>Business taxes are payable on gross receipts and are applicable to sole ownerships, partnerships, and corporations.</p> <p>The gross revenue tax is payable on or before the 30th day following the close of each quarter.</p>	<p>100 percent of wages and salaries of citizens and 50 percent of wages and salaries of noncitizens are allowable deductions.</p>	<p>4 percent on the total after allowable deductions.</p>
Net income tax.	<p>Financial institutions.</p> <p>The net income tax is payable on or before the 30th day following the close of each quarter.</p>	<p>100 percent of wages and salaries of citizens and 50 percent of wages and salaries of noncitizens, interests or discounts paid, ordinary operating expenses such as supplies, utility services, insurance premiums, other than life insurance, provided that any deductible insurance expenses shall be allowable only to the extent that such a premium is applicable to the tax period against which it is claimed; loans or obligations charged against reserves then in existence; losses other than loan losses, such as those occasioned by fire or other casualty, theft, embezzlement, and the like, but only to the extent not covered by proceeds collected; transfers from earnings to reserve for bad debts or other contingencies provided for; miscellaneous direct expenses such as legal, advertising, auditing, and the like; loss on property sold and depreciation on property owned.</p>	<p>4 percent net income.</p>

Table 5a. Republic of Palau: Summary of Tax Structure, 1998/99

Type of Tax	Nature of Tax	Exemptions and Deductions	Rate Structure
Import tax.	Every person who imports products into the Republic of Palau for commercial purposes shall pay import taxes.	Medicines, medical supplies, foodstuff for human consumption, products for government and for personal use are exempt, except for vehicles.	
	Cigarettes.		\$0.50 per 20 sticks.
	Tobacco products, other than cigarettes.		150 percent ad valorem.
	Perfumery, cosmetics, including cologne and other toilet waters, articles of perfumery, and all preparations to the hair and skin, except soap, toothpaste, shampoo, and the like, lipsticks, pomades, powders, and other toilet preparations not having medicinal properties.		25 percent ad valorem.
	Carbonated soft drinks.		\$0.10 per 12 oz.
	Beer.		\$0.03 per oz.
	Liquor.		\$0.30 per oz.
	Wine.		\$0.20 per oz.
	Wine coolers.		\$0.05 per oz.
	Liquid fuel.		\$0.05 per gal.
	Vehicles.		5 percent ad valorem + \$250.00 per vehicle.
	All other imported products.		3 percent ad valorem.
Hotel/Motel room tax.	Every hotel and motel business is required to collect room tax from guests and hold in trust and pay over to the National Treasury.		10 percent of net room charge.
	The room tax is payable on or before the 15th of every month.		
Amusement device tax.	Every person who, at any time during the tax year, owns a coin-activated amusement device for business shall pay an amusement device tax.		\$200.00 per device.
	Tax is payable within 30 days of its purchase or on or before the 31st day of January.		

Table 5a. Republic of Palau: Summary of Tax Structure, 1998/99

Type of Tax	Nature of Tax	Exemptions and Deductions	Rate Structure
Travelers head tax.	Every person departing from the Republic of Palau whether by aircraft or by vessel shall pay a departure tax.	Palauan students, children under the age of 3 and masters, pilots and other crewmembers of aircrafts or vessels are exempt.	\$20.00 per person.
Road use tax.	Every person who owns a motor vehicle shall pay an annual road use tax. Road use tax is based on motor vehicle weight.  Tax is payable at time of registration.	National government and public corporations owned motor vehicles are exempt.	\$50.00 (0-2,000 lbs.) \$75.00 (2,000-4,000 lbs.) \$150.00 over 4,000 lbs.
Foreign water vessel tax.	Every nonresident-owned water vessel entering the Republic of Palau shall be assessed and levied a tax. A nonresident-owned water vessel present in the Republic of Palau for more than one year shall be assessed and levied an annual tax.	U.S. military and common carrier-owned vessels are exempt.	\$50.00 per entry. \$250.00 annual tax.
Fish export tax.	Every person exporting any species of tuna or billfish in any form for commercial purposes shall pay tax.		\$0.25 per kg.
Vessel cabin tax.	A tax levied against paying passengers taking overnight cabin accommodations on ships or water vessels owned or operated by persons or business entities licensed to do business in the Republic of Palau.		10 percent of cabin charge or \$10.00 per day or fraction thereof whichever is greater.

Table 6. Republic of Palau: U.S. Grants, 1994/95-2002/03

(In thousands of U.S. dollars)

	1994/95	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02	2002/03
Under Compact									
Basic grants	21,227	18,622	18,856	19,220	11,762	12,294	12,450	12,605	12,761
Operations	14,948	12,781	12,781	12,781	7,781	7,781	7,781	7,781	7,781
Inflation adjustment	6,279	5,841	6,075	6,439	3,981	4,513	4,669	4,824	4,980
Energy - Section 211(b)	28,000	0	0	0	0	0	0	0	0
Inflation adjustment	12,880	0	0	0	0	0	0	0	0
Trust fund - Section 211(f)	66,000	0	4,000	0	0	0	0	0	0
Capital improvements	36,000	0	0	0	0	0	0	0	0
Inflation adjustment	16,560	0	0	0	0	0	0	0	0
Military options	5,500	0	0	0	0	0	0	0	0
Special program assistance	6,300	4,900	3,500	2,000	2,000	2,000	2,000	2,000	2,000
Total direct payments	192,467	23,522	22,356	21,220	13,762	14,294	14,450	14,605	14,761
Special program assistance									
Federal services									
Road system construction	53,000	0	96,000	0	0	0	0	0	0
Weather, postal, aviation services	1,340	1,490	1,640	1,790	1,940	2,090	2,240	2,390	2,540
Total federal services	54,340	1,490	97,640	1,790	1,940	2,090	2,240	2,390	2,540
Total Compact aid	246,807	25,012	119,996	23,010	15,702	16,384	16,690	16,995	17,301
Other U.S. assistance 1/	16,245	13,360	10,586	8,172	9,558	7,646	6,117	4,894	3,915
Total U.S. grants	263,052	38,372	130,582	31,182	25,260	24,030	22,807	21,889	21,216

Sources: Independent Auditor's Report on Financial Statements; and data provided by the Palauan authorities.

1/ Other U.S. assistance is received based on the proposals submitted to each grantor agency. Based on the Compact agreement, various programs were to phase out beginning fiscal year 1996. Scheduled phasing out is 25 percent reduction of grant authorization for each fiscal year. However, there are available old and new programs for which the Republic of Palau is eligible.

Table 7. Republic of Palau: National Government Expenditure  
by Budget Category, 1992/93-1997/98

(In thousands of U.S. dollars)

	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98
Office of the President	1,013	1,221	1,251	985	1,408	1,645
Office of the Vice-President	330	346	390	410	437	507
<b>Ministries</b>						
State	1,116	1,234	1,627	1,846	1,731	1,859
Administration	2,752	1,578	1,618	2,204	1,953	1,911
Health	...	5,833	7,608	8,030	9,704	9,147
Education	...	9,741	11,204	8,844	9,173	8,833
Community and Cultural Affairs	...	920	1,010	726	654	815
Social Services	15,055	...	...	...	...	...
Justice	1,565	2,030	2,308	2,458	2,973	2,970
Resources and Development	...	8,274	4,736	3,931	4,830	5,534
Commerce and Trade	...	407	810	914	1,559	1,753
Natural Resources	9,597	...	...	...	...	...
<b>Boards, Community, and Authorities</b>						
Office of the Public Auditor	465	598	1,208	835	791	454
Office of the Special Prosecutor	344	378	391	527	608	566
Office of the Special Prosecutor	175	156	136	188	117	62
Olbiil Era Kelulau (Congress)	2,597	3,227	3,470	3,261	3,651	3,384
Grants to State Governments	3,266	3,484	3,268	1,747	4,682	4,612
Judiciary	1,390	1,464	1,618	1,793	1,915	2,045
Other	2,748	4,056	4,260	7,018	6,890	5,204
Capital expenditures	3,792	3,012	8,529	17,003	18,290	9,856
Interest payments	14	0	0	0	0	0
Operating transfers 1/	357	2,422	9,809	12,429	5,176	3,460
Public enterprises	207	266	5,543	7,889	3,036	1,000
Other	150	2,158	4,266	4,540	2,140	2,460
<b>Total</b>	<b>46,576</b>	<b>50,383</b>	<b>65,251</b>	<b>75,148</b>	<b>76,542</b>	<b>64,617</b>

Sources: Reports on the Audit of Financial Statements for fiscal years 1992/93-1997/98 (1997/98 data are preliminary); and data provided by the Palauan authorities.

1/ Includes subsidies and other transfers for current operations.



Table 8. Republic of Palau: Operating Accounts of the State Governments, 1992/93-1995/96

(In thousands of U.S. dollars)

	1992/93	1993/94	1994/95	1995/96
<b>Revenues</b>				
National Government Grant	2,704	2,612	1,303	4,960
Fishing rights fees	669	885	346	847
Interest income	3	2	5	27
Other	481	333	114	853
<b>Total revenues</b>	<b>3,856</b>	<b>3,832</b>	<b>1,768</b>	<b>6,688</b>
<b>Expenditures</b>				
Salaries and wages	650	654	334	1,451
Capital expenditure	637	1,023	399	2,815
Other	2,263	2,395	1,097	1,623
<b>Total expenditures</b>	<b>3,550</b>	<b>4,071</b>	<b>1,830</b>	<b>5,889</b>
<b>Net collection (deficit)</b>	<b>306</b>	<b>-239</b>	<b>-62</b>	<b>799</b>
Fund balance (beginning of year)	384	690	451	390
Fund balance (end of year)	690	451	390	1,189

Source: Data provided by the Palauan authorities.

Table 9. Republic of Palau: Financial Position of the Compact  
Section 211(f) Trust Fund, 1994/95-1998/99

(In thousands of U.S. dollars)

	1994/95	1995/96	1996/97	1997/98	At May 1999
Total receipts	71,034	6,961	28,861	17,599	18,947
Compact grants 1/	66,000	0	4,000	0	0
Investment gains and interest income	5,034	6,961	24,861	17,599	18,947
Total expenditures	255	564	502	773	555
Investment fees	255	564	502	773	555
Overall balance	70,779	6,397	28,359	16,826	18,392
Fund balance at year-end	70,779	77,176	105,536	122,362	140,754

Sources: Independent Auditor's Report on Financial Statement; and data provided by the Palauan authorities.

1/ Covers operations of the Compact Section 211(f) Trust Fund, starting in 1994/95.

Table 10. Republic of Palau: Financial Position of the Social Security Fund, 1992/93-1997/98

(In thousands of U.S. dollars)

	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98
Revenues	4,268	3,349	5,727	4,930	5,328	5,503
Contributions	2,889	3,383	3,615	4,014	5,310	5,487
Government	1,534	1,853	1,948	2,011	2,681	2,644
Private	1,345	1,517	1,649	1,983	2,599	2,805
Penalties and interest	10	13	18	20	30	38
Investment and other income	1,379	-34	2,112	916	18	16
Expenditures	2,312	2,539	2,625	2,871	3,105	2,852
Total benefit payout 1/	1,947	2,192	2,304	2,420	2,616	2,278
Administrative fees 2/	365	347	321	451	489	574
Net collection (deficit)	1,956	810	3,102	2,059	2,223	2,651
Fund balance (end-year)	8,666	9,477	12,579	14,639	19,817	23,254

Sources: Annual Audit Reports; and data provided by the Palauan authorities.

1/ Total benefit payout includes retirements, survivors, disability, and lump-sum payments.

2/ Including administrative and investment management expenses and fees.

Table 11. Republic of Palau: Financial Position of the  
Civil Service Pension Fund, 1992/93-1997/98

(In thousands of U.S. dollars)

	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98
Revenues	4,202	2,715	7,221	5,688	7,069	5,108
Contributions						
Government employees	2,228	2,708	2,851	3,125	3,285	3,309
Investment gains (losses)	992	-359	1,827	653	3,306	1,201
Investment interest income	159	164	227	290	346	456
Other income	672	52	86	120	132	142
Transfers from national government	150	150	2,230	1,500	0	0
Expenditures	2,032	1,840	2,305	2,536	3,025	3,116
Total benefit payout 1/	1,416	1,557	1,980	2,078	2,545	2,703
Administrative fees 2/	616	283	325	458	480	413
Net collection (deficit)	2,170	875	4,915	3,152	4,044	1,992
Fund balance (end-year)	7,422	8,297	13,212	16,364	20,408	22,400

Sources: Independent Auditor's Report on Financial Statements; and data provided by the Palauan authorities.

1/ Including lump-sum benefits, refunds, and disability benefits.

2/ Including investment management expenses and fees.

Table 12. Republic of Palau: Operating Accounts of the Palau Public Utilities Corporation, 1994/95-1997/98

(In thousands of U. S. dollars)

	1994/95	1995/96	1996/97	1997/98
Operating revenues	4,508	5,418	6,231	7,997
Energy charges	4,507	5,295	6,129	7,812
Other	1	123	102	185
Operating expenses	6,555	7,718	9,956	11,805
Salaries, goods, and services	6,538	7,640	9,011	7,859
Depreciation	17	78	945	3,946
Gross operating profit (loss)	-2,047	-2,300	-3,725	-3,808
Capital expenditures	946	3,176	7,890	...
Total profit (loss)	-2,993	-5,476	-11,615	...
Subsidies from government and foreign grants	6,876	7,230	2,239	...
Net total profit (loss)	3,883	1,754	-9,376	...
Provision for depreciation	17	78	945	...
Long-term borrowing	0	90	0	...
Change in fund balances (decrease -)	3,900	1,922	-8,431	...
Memorandum items:				
Cash balance (beginning of year)	-2,294	3,759	6,386	...
Plus: Change in fund balances (decrease -)	3,900	1,922	-8,431	...
Minus: Change in working capital (decrease -)	-2,153	-705	761	...
Equals: Cash balance (end-of-year)	3,759	6,386	-2,806	...

Sources: Independent Auditor's Report on Financial Statements; and data provided by the Palauan authorities.

Table 13. Republic of Palau: Operating Accounts of the  
Palau Housing Authority, 1992/93-1996/97

(In thousands of U. S. dollars)

	1992/93	1993/94	1994/95	1995/96	1996/97
Revenues	297	232	239	474	389
Federal contributions	256	201	188	428	332
Interests	30	20	38	19	13
Others	0	1	3	17	19
Transfers from national government	10	10	10	10	25
Expenditures	324	254	191	441	398
Wages and salaries	34	36	44	45	27
Depreciation	14	16	16	14	15
Interest expense	10	7	6	5	4
Others	267	194	125	376	352
Change in equity during the year	-28	-21	48	59	23
Fund equity, beginning of year	-325	-353	-374	-326	-268
Fund equity, end of year	-353	-374	-326	-268	-245

Sources: Independent Auditor's Report on Financial Statements; and data provided by the Palauan authorities.

Table 14. Republic of Palau: Operating Accounts of the Palau National Communications Corporation, 1992/93-1997/98

(In thousands of U. S. dollars)

	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98
Operating revenues	3,979	4,426	4,668	5,458	5,835	6,390
Sales of goods and services	3,979	4,426	4,668	5,458	5,835	6,390
Operating expenses	2,344	2,608	2,784	3,131	4,496	5,632
Salaries, goods, and services	1,922	2,192	2,303	2,370	3,332	2,836
Depreciation	320	363	469	637	1,065	2,786
Other	102	53	13	124	99	10
Other income (expenses) 1/	6	-89	249	151	-511	-1,153
Change in equity during the year	1,641	1,728	2,132	2,478	828	-403
Fund equity, beginning of year	5,131	6,772	8,500	10,633	13,111	13,939
Fund equity, end of year	6,772	8,500	10,633	13,111	13,939	13,536

Sources: Independent Auditor's Report on Financial Statements; and data provided by the Palauan authorities.

1/ Not related to the normal operation of the corporation and includes adjustments to the fund balance.

Table 15. Republic of Palau: Structure of Interest Rates, May 1997-May 1999  
Bank of Hawaii

(In percent per annum)

	<u>May</u> 1997	<u>May</u> 1998	<u>May</u> 1999
<b>Deposit rates</b>			
Checking account (with minimum balance)	0.00-4.50	0.00-4.51	0.00-4.52
Savings account	2.25-5.00	2.50	2.00
<b>Time savings account</b>			
30 days	3.00-5.00	2.70-3.00	2.30-2.45
One year	4.50-6.00	4.50-4.75	3.40-3.50
<b>Certificates of deposit</b>			
Six months	5	3.75-4.45	3.10-3.20
One year	6	4.50-4.75	3.40-3.50
Two years	7	4.70-4.90	3.70-3.80
Three years	8	4.90-5.05	3.85-3.95
<b>Lending rates</b>			
Consumer loans	15.00-18.00	15	15
Commercial loans (one year) 1/	9.50-12.50	Prime + 4 percent	Prime + 4 percent
<b>Residential housing loans</b>			
30-year, fixed	12	12	12
15-year, fixed	12	12	12

Source: Data provided by the Palauan authorities.

1/ Commercial loan rates follow the highest New York Prime plus 4 percent.



Table 16. Republic of Palau: Structure of Interest Rates, May 1997-May 1999  
Bank of Guam-Palau Branch

(In percent per annum)

	<u>May</u> 1997	<u>May</u> 1998	<u>May</u> 1999
<b>Deposit rates</b>			
Checking account (with minimum balance)	0.00-2.25	0.00-2.00	0.00-2.00
Savings account	2.25-3.00	2.25-3.00	2.25-3.00
<b>Time savings account</b>			
30 days	2.25-3.00	2.25-3.00	2.25-3.00
One year	2.25-3.25	2.25-3.25	2.25-3.25
<b>Certificates of deposit</b>			
Six months	4.12-4.25	4.10-4.47	3.02-3.39
One year	4.18-4.31	4.14-4.64	3.28-3.60
Two years	4.25-4.37	4.36-4.86	3.35-3.72
Three years	4.31-4.50	4.36-4.86	3.75-3.94
<b>Lending rates</b>			
Consumer loans	15.00-18.00	15.00-18.00	15.00-18.00
Commercial loans (one year)	10.50-12.75	10.50-12.75	9.75-12.50

Source: Data provided by the Palauan authorities.

Table 17. Republic of Palau: Operating Accounts of the National Development Bank of Palau, 1992/93-1997/98

(In thousands of U. S. dollars)

	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98
Revenues	424	535	2,675	1,875	871	821
Loan fees	304	370	397	547	746	770
Other	11	20	58	52	126	50
Transfers from national government	58	95	219	276	0	0
Contributions from other countries	50	50	2,000	1,000	0	0
Expenditures	255	435	493	570	602	256
Wages and salaries	103	117	107	138	136	123
Depreciation	11	13	23	19	16	13
Interest	32	33	36	17	0	5
Other	110	272	327	395	450	115
Net income (losses)	169	100	2,182	1,305	270	564
Fund equity (beginning of year)	836	1,004	1,104	3,287	4,592	4,862
Fund equity (end of year)	1,004	1,104	3,287	4,592	4,862	5,426

Sources: Independent Auditor's Report on Financial Statements; and data provided by the Palauan authorities.

Table 18. Republic of Palau: Assets and Liabilities of the National Development Bank of Palau, 1992/93-1997/98

(In thousands of U.S. dollars; end of period)

	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98
<b>Assets</b>						
Cash	537	707	1,775	1,146	33	113
Time certificates of deposit	0	100	500	600	606	1,339
Loans	2,519	2,487	2,721	4,356	5,728	5,049
Fixed assets	44	59	52	36	25	33
Other 1/	7	31	50	38	33	46
<b>Total assets</b>	<b>3,107</b>	<b>3,384</b>	<b>5,098</b>	<b>6,176</b>	<b>6,425</b>	<b>6,580</b>
<b>Liabilities</b>						
Accounts payable 2/	88	28	18	23	1	8
Bonds payable	0	253	0	0	0	0
Loans payable	900	885	680	407	407	0
Bank capital 3/	2,119	2,218	4,400	5,746	6,016	6,572
<b>Total liabilities</b>	<b>3,107</b>	<b>3,384</b>	<b>5,098</b>	<b>6,176</b>	<b>6,425</b>	<b>6,580</b>

Sources: Independent Auditor's Report on Financial Statement; and data provided by the Palauan authorities.

1/ Includes other receivables, inventory, and prepaid expenses.

2/ Includes accrued expenses.

3/ Includes contributed capital and retained earnings.

Table 19. Republic of Palau: Credit Allocation by the National Development Bank of Palau, 1992-98

(In thousands of U.S. dollars)

	1992	1993	1994	1995	1996	1997	1998
Agriculture	56.9	23.4	47.3	54.6	65.0	45.0	7.0
Fisheries	237.8	270.9	239.4	201.6	359.0	164.0	16.0
Tourism	910.2	867.3	1,259.1	1,257.8	348.0	265.0	0.0
Forestry	4.4	0.2	0.0	0.0	0.0	0.0	0.0
Manufacturing	91.5	1.8	1.7	0.0	48.3	0.0	0.0
Commerce and construction	1,411.9	1,640.5	1,353.8	1,789.6	2,469.0	1,685.0	70.0
Total loans	2,712.7	2,804.1	2,901.4	3,303.5	3,289.3	2,159.0	93.0

Source: Data provided by the Palauan authorities.

Table 20. Republic of Palau: Balance of Payments, 1992/93-1997/98

(In thousands of U.S. dollars)

	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98
Trade balance	-24,470	-31,659	-46,569	-58,517	-61,079	-52,126
Exports, f.o.b.	17,739	12,582	13,868	13,907	11,814	11,095
Imports, f.o.b. 1/	-42,209	-44,240	-60,438	-72,424	-72,894	-63,222
Services account	5,889	17,023	23,958	34,447	41,203	40,292
Receipts	17,698	29,429	40,554	54,213	61,220	58,003
Travel 2/	17,698	29,429	40,554	54,213	61,220	58,003
Payments	-11,808	-12,406	-16,596	-19,766	-20,017	-17,711
Freight and insurance 3/	-10,552	-11,060	-15,109	-18,106	-18,223	-15,805
Travel	-1,256	-1,346	-1,487	-1,660	-1,793	-1,906
Income	3,202	-177	10,458	10,159	17,857	6,619
Investment income	3,202	-177	10,458	10,159	17,857	6,619
Interest payment	0	0	0	0	0	0
Current transfers	23,622	23,032	80,499	26,558	23,680	22,382
Private	-4,826	-5,745	-4,817	-5,408	-6,404	-6,062
Inflows	736	797	880	983	1,062	1,129
Outflows	-5,562	-6,542	-5,698	-6,391	-7,466	-7,190
Official	28,448	28,777	85,317	31,966	30,084	28,444
Fishing rights	855	931	1,001	1,000	867	800
Grants	27,592	27,845	84,643	31,060	29,598	28,435
Other 4/	0	0	-327	-95	-381	-791
Current account (incl. official grants)	8,243	8,219	68,346	12,647	21,661	17,167
Current account (excl. official grants)	-19,350	-19,626	-16,297	-18,413	-7,937	-11,268
Capital and financial account	3,792	12,671	57,129	4,974	174	-2,054
Capital grants 5/	3,792	12,671	61,629	7,974	3,574	1,546
Loan repayments 6/	0	0	-4,500	-3,000	-3,400	-3,600
Errors and omissions	-12,273	-21,270	-29,165	-29,838	-24,917	-11,017
Overall balance 7/	-239	-380	96,310	-12,217	-3,082	4,096
Memorandum items:						
Imports/GDP (in percent)	56	52	57	58	56	49
Trade account/GDP (in percent)	-32	-37	-44	-47	-47	-40
Current account/GDP (in percent)						
Including official grants	11	10	65	10	17	13
Excluding official grants	-26	-23	-15	-15	-6	-9

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

1/ Includes government and tax-exempt imports.

2/ Estimated on the basis of official data on the number of visitors to Palau, and data on average length of stay and average daily spending.

3/ Estimated to have amounted to 25 percent of the f.o.b. value of imports.

4/ Contribution to international and regional organizations.

5/ Grants received for capital improvements.

6/ Principal payment on external debt.

7/ Reflects the changes in the financial holdings of the government excluding Compact Section 211(f) Trust Fund.

Table 21. Republic of Palau: Imports by Product Category, 1994-97 1/

( In thousands of U.S. dollars; f.o.b.)

	1994	1995	1996	1997	Average 1994-97
Food and live animals	6,647	9,164	9,317	10,987	9,029
Percent share of total	14	15	12	16	14
Beverages and tobacco	3,816	5,002	5,428	6,165	5,103
Percent share of total	8	8	7	9	8
Crude materials, inedible except fuels	33	187	118	199	134
Percent share of total	0	0	0	0	0
Mineral fuels, lubricant, and related minerals	19,882	15,057	20,886	8,341	16,041
Percent share of total	41	24	26	12	25
Animal and vegetable oils, fats, and waxes	112	234	204	268	204
Percent share of total	0	0	0	0	0
Chemicals and related products	1,147	2,306	1,949	2,818	2,055
Percent share of total	2	4	2	4	3
Manufactured goods	3,546	4,765	4,930	5,713	4,738
Percent share of total	7	8	6	8	7
Machinery and transport equipment	5,936	13,246	23,846	17,599	15,157
Percent share of total	12	21	30	25	23
Misc. manufactured articles	7,100	12,567	12,758	17,148	12,393
Percent share of total	15	20	16	25	19
Commodities and transactions not classified elsewhere	363	191	199	51	201
Percent share of total	1	0	0	0	0
<b>Total</b>	<b>48,582</b>	<b>62,719</b>	<b>79,636</b>	<b>69,289</b>	<b>65,057</b>

Source: Data provided by the Palauan authorities.

1/ On a calendar-year basis.

Table 22. Republic of Palau: Imports by Origin, 1996-97 1/

( In thousands of U.S. dollars; f.o.b.)

	1996	1997
United States	27,010	27,872
Percent share of total	34	40
Guam	12,473	12,223
Percent share of total	16	18
Japan	9,051	9,348
Percent share of total	11	13
Singapore	23,412	9,047
Percent share of total	29	13
Taiwan	2,391	3,465
Percent share of total	3	5
China	42	1,685
Percent share of total	0	2
Hong Kong	1,070	1,245
Percent share of total	1	2
Philippines	1,053	1,221
Percent share of total	1	2
Australia	1,463	994
Percent share of total	2	1
Saipan	440	690
Percent share of total	1	1
New Zealand	238	590
Percent share of total	0	1
Korea	570	517
Percent share of total	1	1
Other countries and territories:	423	391
Percent share of total	1	1
Total	79,636	69,289

Source: Data provided by the Palauan authorities.

1/ On a calendar-year basis.

Table 23. Republic of Palau: Tourism and Business Arrivals, 1993-99 1/

(In number of arrivals, by country of citizenship, except as otherwise indicated)

	1993	1994	1995	1996	1997	1998	Jan.-Mar. 1999 2/
Taiwan Province of China	3,384	5,559	10,727	22,523	30,497	18,396	1,897
Percent change over previous period	...	64.3	93.0	110.0	35.4	-39.7	-69.2
Percent share of tourist and business arrivals	9.9	14.8	22.8	37.1	45.9	31.2	14.4
Japan	18,095	16,939	20,202	21,410	19,519	21,191	6,984
Percent change over previous period	...	-6.4	19.3	6.0	-8.8	8.6	6.5
Percent share of tourist and business arrivals	53.2	45.1	43.0	35.3	29.4	35.9	53.1
United States	7,080	8,837	9,017	8,878	9,400	11,616	2,550
Percent change over previous period	...	24.8	2.0	-1.5	5.9	23.6	-3.3
Percent share of tourist and business arrivals	20.8	23.5	19.2	14.6	14.1	19.7	19.4
Korea	831	1,163	1,738	1,907	1,640	498	129
Percent change over previous period	...	40.0	49.4	9.7	-14.0	-69.6	19.4
Percent share of tourist & business arrivals	2.4	3.1	3.7	3.1	2.5	0.8	1.0
Australia and New Zealand	523	446	634	1,212	500	500	122
Percent change over previous period	...	-14.7	42.2	91.2	-58.7	0.0	90.6
Percent share of tourist and business arrivals	1.5	1.2	1.3	2.0	0.8	0.8	0.9
Philippines	1,092	980	627	854	879	630	71
Percent change over previous period	...	-10.3	-36.0	36.2	2.9	-28.3	-56.7
Percent share of tourist and business arrivals	3.2	2.6	1.3	1.4	1.3	1.1	0.5
Other	3,036	3,654	4,078	3,935	4,006	6,177	1,405
Percent change over previous period	...	20.4	11.6	-3.5	1.8	54.2	6.1
Percent share of tourist and business arrivals	8.9	9.7	8.7	6.5	6.0	10.5	10.7
Total tourism and business arrivals	34,041	37,578	47,023	60,719	66,441	59,008	13,158
Percent change over previous period	...	10.4	25.1	29.1	9.4	-11.2	-22.6
Total arrivals 1/	40,497	44,073	53,229	69,330	73,719	64,194	15,409
Percent change over previous period	...	8.8	20.8	30.2	6.3	-12.9	-17.2

Source: Data provided by the Palauan authorities.

1/ Includes returning residents, fishermen, crews, students, transits, and dependents.

2/ Percentage change in arrivals is calculated in relation to the first quarter of 1998.



Table 24. Republic of Palau: National Government Debt and Debt Service, 1992/93-1999/2000

(In thousands of U.S. dollars)

	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98	1998/99	1999/2000
External debt	67,429 1/	20,000 1/	15,500	12,500	9,100	5,500	1,433	0
Debt service								
Principal 2/	0	0	4,500	3,000	3,400	3,600	4,067	1,433
Interest 2/	0	0	0	0	0	0	0	0

Sources: Independent Auditor's Report on Financial Statements; and data provided by the Palauan authorities.

1/ Total external debt outstanding (related to the construction of IPSECO power plant), including payments arrears.

2/ In June 1993, an agreement was reached with the guarantor banks for the settlement of the outstanding IPSECO debt, by which there would be debt relief and only \$20 million would be paid to the guarantor banks over the period 1994/95-1999/2000 without any interest payment.