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NEWS: Africa's oil wealth raises stakes for transparency

With the rapidly growing importance of natural resource wealth in many African economies, the IMF and the World Bank have stepped up efforts to help countries avoid the "resource curse." Transparency and accountability are key tools in ensuring that living standards rise for all citizens, not just for the select few. An IMF–World Bank workshop in Malabo, Equatorial Guinea, for regional and national parliamentarians put the spotlight on best practices in resource management.

Simon Willson/IMF

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REGIONAL FOCUS: Shaking off East Caribbean's doldrums

Can the Eastern Caribbean region—traditionally prone to hurricanes and increasingly buffeted by the strong winds of global economic forces—shake off sluggish growth and rising debt? A recent seminar, cosponsored by the IMF's Western Hemisphere Department and the Eastern Caribbean Central Bank, took a hard look at what the island economies with their small populations and scant natural resources can do to weather debt woes and revive their economic fortunes.

Stephen Jaffe/IMF

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FORUM: Is China's renminbi out of line?

In the past year, China has come under increasing international pressure to adopt more flexible currency policies. The IIE's Morris Goldstein argues that China's exchange rate policy is flawed given the country's macroeconomic circumstances and longer-term economic policy goals. A reform of China's currency policies would be in its own best interest—to avoid further excessive credit growth and overheating as well as the risk that rising protectionist pressures in the West could cause it to lose some of its market access.

Michael Spilotro/IMF

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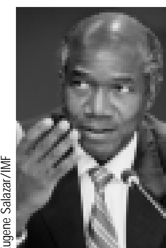
OUTREACH: IMF and the fight against HIV/AIDS

To counter misperceptions that it holds back critical spending on HIV/AIDS, the IMF held a workshop for donors, international agencies, and NGOs, with a focus on Honduras, Kenya, Uganda, and Zambia. IMF staff explained that IMF programs do not contain hard ceilings on health care spending. Participants suggested that budget discussions should be opened up to more stakeholders and that the IMF could do more to reassure countries that new spending can be accommodated.


Eugene Salazar/IMF

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What's on

February

15–16 Conference on "Macroeconomic Challenges in Low-Income Countries," IMF, Washington, D.C.

15–16 Symposium: Whither Development Economics? IMF, Washington, D.C.

16 IMF Managing Director Rodrigo de Rato begins visit to Colombia, Ecuador, Bolivia, and Peru

18 Deadline for public comments on the IMF's draft *Guide on Resource Revenue Transparency*

23–24 IMF–Arab Monetary Fund, Seminar on "Arab Economic Integration: Challenges and Prospects," Abu Dhabi

28–March 11 Beijing+10 Conference: 49th Session of the Commission on the Status of Women, United Nations, New York

March

14–15 IMF Seminar on Foreign Aid and Macroeconomic Management, Maputo, Mozambique

16 OPEC: 135th Meeting of the Conference, Isfahan, Iran

17–18 IMF seminar for legislators, Dili, Timor-Leste

20–21 OECD: China in the World Economy: China Development Forum 2005, Beijing, China

23–24 IMF seminar for legislators, Phnom Penh, Cambodia

April

5 IMF's *Global Financial Stability Report* (April 2005) released

10–12 Inter-American Development Bank Annual Meeting, Okinawa, Japan

13 IMF's *World Economic Outlook* (Spring 2005) released

16–17 2005 Spring Meetings of the IMF and the World Bank Group, Washington, D.C.

IMF Executive Board

For an up-to-date listing of IMF Executive Board meetings, see *http://www.imf.org.external/np/sec/bc/eng/index.asp.*

IEO deadline for input

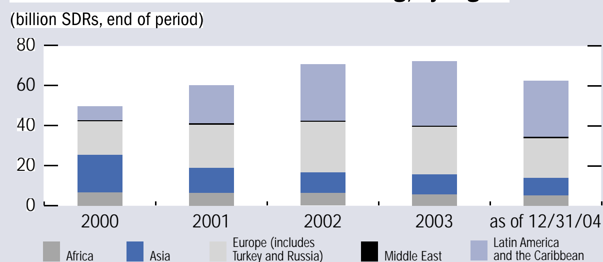
The IMF's Independent Evaluation Office is seeking suggestions on future topics for evaluation. Comments are requested by February 15. For further information, including a preliminary list of possible topics, see: *http://www.imf.org/external/np/ieo/index.htm*

At a glance

IMF financial data

Total IMF credit and loans outstanding, by region

(billion SDRs, end of period)

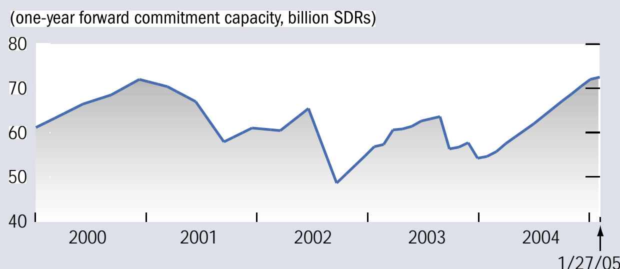


Major currencies, rates per SDR

	February 1, 2005	Year ago
Euro	1.167	1.192
U.K. pound	0.807	0.815
Japanese yen	157.496	156.877
U.S. dollar	1.519	1.485

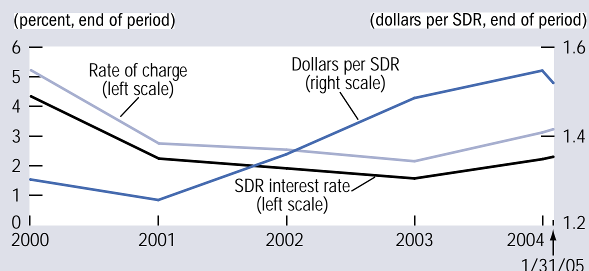
IMF available resources

(one-year forward commitment capacity, billion SDRs)



Related rates

SDR interest rate, rate of charge on IMF nonconcessional loans outstanding, and dollars per SDR



Note on IMF Special Drawing Rights

Special Drawing Rights (SDRs) are an international reserve asset, created by the IMF in 1969 to supplement the existing official reserves of member countries. SDRs are allocated to member countries in proportion to their IMF quotas. The SDR also serves as the unit of account of the IMF and some other international organizations. Its value is based on a basket of key international currencies.

Africa's oil wealth raises the stakes for transparency

As more African countries debate the benefits and the pitfalls of their newfound oil wealth, questions of fiscal transparency and accountability are gaining increased urgency. A one-day workshop in Malabo, Equatorial Guinea, January 27, organized by the IMF and the World Bank, took up the topic, with parliamentarians from the six countries of the Economic and Monetary Community of Central African States (CEMAC)—Cameroon, the Central African Republic, the Republic of Congo, Chad, Equatorial Guinea, and Gabon—and Equatorial Guinea's national parliamentarians.

Transparency in oil resource management was once virtually a taboo topic. To have it as the theme of a workshop, observed CEMAC Interparliamentary Commission President Batho Obam Nsue Mangue, is itself revolutionary. But, as IMF Deputy Managing Director Agustín Carstens told the legislators, transparency and accountability are now seen as essential for ensuring that resource wealth is used for the benefit of the whole of a country's population. Carstens highlighted recent international initiatives, including the IMF's *Guide on Resource Revenue Transparency* (see related story, page 21). He underscored that adhering to principles of transparency and accountability can translate to better economic results—citing Botswana's handling of diamond production revenues, which has also been conducive to business and investment in the nondiamond sector; the Republic of Congo's quarterly external audits of government oil revenues; and Nigeria's publication of the financial results of oil licensing rounds.

Equatorial Guinea's President, Teodoro Obiang Nguema Mbasogo, told participants that he believed the event would better prepare parliaments to ensure the transparent use of the region's economic resources. He added that the choice of Equatorial Guinea as the host of the seminar reflected the determination of his government in particular—and of Central African countries in general—to enhance the transparent management of public resources for the benefit of their people.

In their discussions with IMF and World Bank staff, the legislators took up a range of resource-related topics. They examined the macroeconomic implications of oil resources in the region, observing that the oil sector was the dominant industry in most CEMAC countries. They explored the respective roles of regional and national parliaments, government agencies, and other stakeholders in the management of oil resources and in determining how oil revenues should be spent. Also debated were ways in which the non-oil sectors of the economy could be fostered and the importance of the Group of Eight's transparency and anticorruption declaration and the Extractive Industries Transparency Initiative for the Gulf of Guinea countries. ■

Simon Willson/IMF

Opening panelists at the Malabo workshop were (l-r) CEMAC Executive Secretary Jean Nkuete; IMF Deputy Managing Director Agustín Carstens; Equatorial Guinea's House of Representatives President Salomon Nguema Owono, President Teodoro Obiang Nguema Mbasogo, and Prime Minister Miguel Abia Biteo Borico; and CEMAC Interparliamentary Commission President Batho Obam Nsue Mangue.

Simon Willson
IMF External Relations Department

Russia pays off IMF debt early

On January 31, Russia ceased being one of the IMF's five largest debtor countries when it repaid its remaining $3.33 billion debt. "Russia's ability to repay the IMF ahead of schedule reflects its strong fiscal and balance of payments position against a background of high oil prices," said IMF Managing Director Rodrigo de Rato. The loans had been contracted under a 1996 Extended Arrangement totaling about $20.1 billion, of which Russia had drawn about $8.8 billion. Under the original repayment schedule, final payment would have been due in 2008.

On the same day it paid off the debt, Russia became a subscriber to the IMF's Special Data Dissemination Standard (SDDS). Created in 1996 by the IMF, the SDDS helps guide countries that have, or might seek, access to international capital markets in providing timely and comprehensive economic and financial data to the public. ■

Sierra Leone's better security buoys economic growth

Sierra Leone's improved security situation helped lay the foundation for broad-based economic growth in recent years, while inflation remained moderate. In 2003, the economy enjoyed a robust recovery, reflecting healthy activity in agriculture, mining, manufacturing, and services, the IMF said in its regular economic assessment. As part of Sierra Leone's post-conflict transition, in February 2004 the government concluded the disarmament, demobilization, and reintegration of more than 72,000 former combatants. The IMF's Executive Board endorsed the medium-term growth and poverty reduction strategy, which focuses on strengthening state security, attaining a more sustainable fiscal position, raising domestic savings and investment, strengthening infrastructure, further developing agriculture and rural areas, and promoting the private sector.

Medium-term growth projections of 6–7 percent annually in 2005-07 are largely based on some mining projects, agricultural expansion, and service-related activities. The Board said the main risk to medium-term growth was insufficient savings and investment. It encouraged the government to continue implementing structural reforms and improving governance to attract domestic and foreign investors.

Inflation is expected to revert to low single digits, and the current account deficits are expected to narrow. The Board expressed concern that inflation, initially resulting from higher fuel costs, was later driven by expansionary monetary policy and a depreciating currency. It recommended tightening monetary policy, including a reduction in government bank borrowing, and supported maintaining the floating exchange rate system.

Fiscal performance in 2003 was marked by higher-than-programmed domestic financing of the budget resulting from a large shortfall in external financing. The Board encouraged the government to tighten fiscal policy, but to preserve, as much as possible, spending for poverty alleviation.

Sierra Leone	2001	2002	2003	2004	2005
		Estimates		Projections	
		(percent change)			
Real GDP	17.9	27.5	9.3	7.4	9.4
Consumer prices (period average)	2.6	–3.7	8.2	13.6	7.3
		(percent of GDP)			
Government budget					
Domestic revenue	13.0	12.1	12.4	12.2	12.9
Total expenditure and net lending	29.5	28.6	26.9	28.8	26.3

Data: IMF staff report.

Kyrgyz Republic's economy grows steadily, but debt still high

Solid economic growth, low inflation, and sound fiscal and monetary policies in the Kyrgyz Republic helped to put poverty on a downward path in recent years, the IMF said in its regular economic assessment. But external public debt has remained high despite a gradual reduction to below 100 percent of GDP. Outside the Kumtor gold mine and the energy sector, real GDP has grown steadily around 4 percent since 2000, while the official poverty rate has fallen to 41 from 52 percent.

Annual inflation has declined since 2000, and the external current account deficits in 2002 and 2003 were about 2.5 percent of GDP with imports and exports growing rapidly. The IMF's Executive Board urged the government to continue fiscal discipline, while ensuring adequate spending on poverty reduction. The 2001–04 Paris Club debt rescheduling had allowed for more pro-poor and social spending. However, further Paris Club debt relief may be necessary. The Board stressed that reaching and maintaining debt sustainability also required a prudent debt strategy, sound macroeconomic policies, and structural reforms. Energy sector reform needs to be accelerated to improve cost recovery, in particular through further measures such as tariff increases.

The general government fiscal deficit gradually declined from 5.5 percent in 2002 toward the 4.5 percent target in 2004, in part thanks to higher tax revenues. The Board encouraged the government to broaden the tax base, improve tax administration, overhaul the tax code, simplify small business taxation, and gradually reduce the payroll tax rate. The exchange rate has been broadly stable, and the Board praised the central bank's monetary and exchange rate management. While the managed float exchange rate regime remains currently appropriate, the Board encouraged the authorities to allow more exchange rate flexibility if warranted by market forces. Further, it stressed the need for strengthening central bank independence and deepening financial markets.

Kyrgyz Republic	2000	2001	2002	2003
		(percent change)		
Real GDP growth	5.3	5.4	0.0	6.7
Consumer prices (period average)	18.7	6.9	2.1	3.1
		(percent)		
Poverty rate	52	48	44	41
		(percent of GDP)		
External public debt	111	100	99	94

Data: IMF staff report.

For more information, refer to Public Information Notices No. 05/4 (Kyrgyz Republic) and 05/5 (Sierra Leone) on the IMF's website (*www.imf.org*)

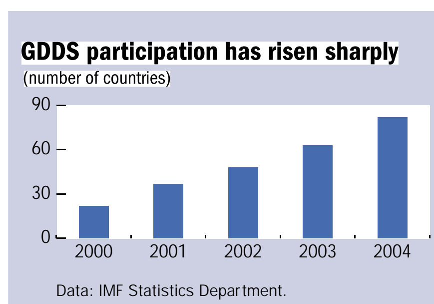
Joining the good data club

Participation in the IMF's General Data Dissemination System (GDDS) has nearly quadrupled over the past four years as countries have sought to improve data quality and establish their credentials as providers of comprehensive, timely, and reliable statistics. Created in 1997, the GDDS now has 83 participating countries (chart) and may see 10 more countries join in 2005. Its data framework is also being put to new use in the fight against poverty and in helping countries to meet the UN Millennium Development Goals.

Why countries join

In adopting the GDDS, countries make a public commitment to develop their national statistical systems. Participation in the system can help form the backbone of a country's statistical efforts, as was the case in China, where the GDDS has helped strengthen transparency and, as Deputy Commissioner of the National Bureau of Statistics Qiu Xiaohua noted, the country's strategic plan of statistics is now closely interrelated to the GDDS framework.

In Kazakhstan, the decision to join the GDDS coincided with a reform of the country's statistical system and the introduction of international principles for disseminating statistical data. The GDDS became a stepping-stone to Kazakhstan's subsequent subscription to the Special Data Dissemination Standard (SDDS), which is intended for countries seeking access to international capital markets. China, too, is working toward subscribing to the more rigorous SDDS.



Data: IMF Statistics Department.

Participation in the GDDS can raise the status of the national statistical office and transform the role that statistics play in the activities of other government agencies. Stepan Mnatsakanyan, President of Armenia's National Statistical Service, saw the GDDS playing a particularly important role in transition countries. In Armenia, he said, the role of the national statistical office shifted from "provider of statistics to the government to a provider of statistics to the whole society."

The GDDS has allowed data-producing agencies to take control of the statistical development program in a structured way and coordinate this program among data-producing agencies, users, donors, and the international community. The GDDS also helps national authorities facilitate resource allocation and ensure that technical assistance complements national initiatives.

Since good statistics are a core component of good governance, GDDS encourages participants to improve the dissemination of their statistics and the compilation of their methodology, and provide contact information to the public. The Internet site of the GDDS—the Dissemination Standards Bulletin Board—then conveys information on statistical development and dissemination practices to the public. For many developing countries, the GDDS site is the only comprehensive source of such information.

Going forward

In the coming year, the IMF's Statistics Department will help potential participants in the GDDS assess their data compilation and dissemination practices and provide technical assistance to improve data quality. Consistent with the IMF's broader objectives of helping low-income countries reach the Millennium Development Goals, the focus will be on encouraging countries with a poverty reduction strategy to participate in the GDDS.

The link between good data and good policies is increasingly being recognized in countries that are crafting ambitious efforts to reduce poverty and raise living standards. When Tajikistan became the 81st country to participate in the GDDS, the chair of the State Committee on Statistics, Munim Kholikov, pointed out that his country's poverty reduction strategy paper (PRSP) explicitly acknowledges the vital role that relevant and reliable statistics play in monitoring and assessing the effectiveness of this strategy.

Developing a PRSP is a very data-intensive process, and currently 44 of the 55 countries that have issued PRSPs participate in the GDDS. The Statistics Department wants to elevate the data quality issue into the mainstream of development work to make the fullest use of the GDDS framework. Countries are encouraged to explicitly prescribe their data development needs and strategies in their PRSPs, similar to what countries are doing for other sectors that require structural reforms. Sierra Leone's PRSP has gone a step further, providing a separate section on statistical development entitled "Empowerment with Information" in its chapter on good governance.

Finally, and perhaps most important, efforts to improve data quality must be adequately funded, and this will require support from the political process, senior-level national officials, statistical agencies, international organizations, and donor countries. ■

Wipada Soonthornsima
IMF Statistics Department

A guide to avoiding the "resource curse"

It's a tale oft told: a wealth of natural resources; staggering increases in public revenues; greed, bribery, and corruption on a massive scale; and a country that stays mired in absolute poverty. It is a tale, though, that can have another ending, and the IMF is seeking to add a new chapter to the story with the release of its draft *Guide on Resource Revenue Transparency.*

A Nigerian government official recently estimated that, notwithstanding recent improvements, corruption and mismanagement still swallow as much as 40 percent of Nigeria's $20 billion annual oil income, while nearly three-quarters of the country's population continues to live below the poverty line. This problem—the resource curse—is not unique to Nigeria. Oil, gold, diamonds, and other resources have bred corruption and even conflict more often than they have spurred development or reduced poverty.

But it doesn't have to be that way. Countries as diverse as Botswana and Norway have shown that good policies and a high degree of transparency can make a difference and help translate resource wealth into higher standards of living and greater investments in health and human capital, along with promoting macroeconomic stability and growth.

The key role that transparency plays in good governance and governmental accountability prompted the IMF to tap its experience in developing a *Code of Good Practices on Fiscal Transparency* (Box 1) and adapt this experience to the specific needs of countries that have great natural resources and wish to avoid the "resource curse." Over the past year, the IMF has been working on specific guidelines on how resource-rich countries can improve fiscal transparency. This effort has come together in a draft *Guide on Resource Revenue Transparency* that is now available for public comment (Box 2).

Box 1

The IMF's fiscal transparency code

Fiscal transparency involves providing ready access to reliable, comprehensive, timely, understandable, and internationally comparable information on government activity, so the public and financial markets can accurately and easily assess the government's financial position, as well as the true costs and benefits of its activities. The IMF's fiscal transparency code covers 37 areas of good practice under the following four general principles: clarity of roles and responsibilities; public availability of information; open budget preparation, execution, and reporting; and external assurances of integrity.

The fiscal transparency code and *Manual on Fiscal Transparency* are available in printed form and on the IMF website in various languages (see *http://www.imf.org/external/standards/index.htm*). For more information, see also *http://www.imf.org/external/np/fad/trans/index.htm.*

Why transparency matters

Of course, this interest in transparency is not new. After financial and political crises in the second half of the 1990s made it clear that markets and voters demanded greater transparency, the IMF launched a broad initiative to develop accepted international standards and agreed-upon codes of conduct in key areas, including fiscal practices. As part of its traditional surveillance of country economic policies, the IMF had always preached the wisdom of sound fiscal policy, but in more recent years it has also increasingly stressed transparency, accountability, and governance.

In 1998, the IMF developed, and encouraged countries to subscribe to, a voluntary code of fiscal transparency. The fiscal transparency code has become a widely recognized international standard and analytical framework and is used by other institutions and organizations (for example, Oxford Analytica) to undertake fiscal transparency assessments. Fiscal transparency reports—part of the broader Reports on the Observance of Standards and Codes (ROSCs)—have been published on the IMF's website for more than 70 member countries. These ROSCs assess country practices against those described in the fiscal transparency code and suggest priorities for improvement.

Resource-rich countries

While fiscal transparency matters for all economies, it may be particularly critical in economies highly dependent on oil and gas reserves that are subject to dramatic price volatility. Around 50 of the IMF's 184 member countries can be considered rich in hydrocarbon and mineral resources. Many of these are low- or middle-income countries in which revenues from these resources account for over 50 percent of government revenue or export proceeds. Revenues from natural resources often pose special challenges to governments in low- or middle-income countries with limited institutional capacity. Given the macroeconomic relevance of these challenges, they are of concern to the IMF.

The draft *Guide on Resource Revenue Transparency* is meant to contribute to the IMF's dialogue with member countries and help them address the numerous challenges associated with pru-

Marshall Wolfe/EPA

Nigerian Liquefied Natural Gas facility. Transparency and accountability are key to translating resource wealth into higher living standards for a country.

dent fiscal management of revenues from extractive industries such as oil, natural gas, and mining. A central message of the *Guide* is that stronger institutions and more transparent resource management practices can significantly benefit governments and taxpayers by promoting more informed public debates over policy options and fostering sounder fiscal policies.

Good practices

The draft *Guide* advocates specific good practices under the four general principles of the fiscal transparency code:

Clarity of government roles and responsibilities. Governments should, for example, establish a clear legal and regulatory framework for the resource sector, covering all production stages and including licensing procedures, production-sharing contracts, and the fiscal regime (for example, royalties and other taxes). The draft *Guide*'s best practices also underscore the need to clarify relations between governments and state-owned enterprises, make the management of resource revenue savings an integrated element of fiscal policy, and establish resource revenue-sharing arrangements between central and local governments.

Public disclosure of resource revenue data and other relevant information. Many resource-rich countries can make quick and highly visible progress in this area and demonstrate their commitment to better transparency. The draft *Guide* recommends publishing all government resource revenues in budget and other reports. Governments should also disclose data on debt and other liabilities related to resource sector operations, financial assets, and information on noncommercial (quasi-fiscal) activities of state-owned enterprises, such as selling energy products below cost recovery or providing social services and infrastructure.

Open processes in budget preparation, execution, and reporting. Governments need to make clear policy statements on the use of natural resource revenues. Governments should also monitor a fiscal balance that excludes resource revenues to help them track fiscal policy performance. Budget documents should explain price and other relevant risks, as well as hedging policies and other measures that are being taken to address these risks. Systems and policies on accounting and internal control and audit should be transparent, and applied as elsewhere in the public sector. Domestic and international resource companies should be subject to the same tax administration framework as other companies, and this framework should be clear and cover all aspects related to taxpayers' rights and obligations, revenue administration powers, and dispute resolution processes.

Independent assurances of integrity with regard to resource-related transactions. Natural resource and other companies need to comply fully with internationally accepted standards for accounting, auditing, and publication of accounts. A national audit office or another independent national organization should verify and report regularly to parliament on revenue flows between companies and the government.

In addition to developing the *Guide*, the IMF has been engaged in a number of complementary activities, including supporting the Extractive Industries Transparency Initiative (EITI), launched by U.K. Prime Minister Tony Blair at the Johannesburg World Summit of Sustainable Development in September 2002. The IMF's ongoing country work combined with other international initiatives has encouraged a number of resource-rich countries to introduce transparency-oriented reforms. Countries such as Azerbaijan and Ghana have participated in fiscal transparency ROSCs. More broadly, there is rising optimism that resource-rich countries will be able to put a greater share of the proceeds from their natural resources to work to further socioeconomic development. Nigeria, for example, is now among the most active participants in the EITI and is working with IMF staff to implement practices that the draft *Guide* recommends. ■

Bill Allan and Günther Taube
Fiscal Affairs Department

Box 2

Public comments invited

The IMF is welcoming comments on its draft *Guide on Resource Revenue Transparency.* The complete text is available on the IMF's website (*http://www.imf.org/external/np/fad/2004/grrt/eng*). Comments should be e-mailed by February 18, 2005 to rrt@imf.org.

How competitive is Poland?

Over the past decade, the Polish economy has generally retained its external competitiveness, and, overall, exports have boomed. But movements in the real exchange rate have not made for a smooth path, and substantial structural changes have left the country with high and persistent unemployment. A recent IMF study took a closer look at Poland's competitiveness and its implications for policymakers.

In terms of several frequently used yardsticks, Poland's external competitiveness in 2004 was broadly comparable with its position in the mid-1990s when the country's external current account deficit was low and export growth strong. Judged by Poland's real effective exchange rate vis-à-vis its trading partner countries (based on consumer price indices and producer price indices), the country saw an appreciation of 2 to 3 percent a year between end–1994 and mid–2004. A real appreciation can be expected during transition periods, and it need not imply a deterioration in competitiveness to the extent that there are "equilibrium effects"—that is, faster productivity growth in the tradable than in the nontradable sector. The average 2 percent a year depreciation of the real effective exchange rate based on unit labor costs during the same period supports this view.

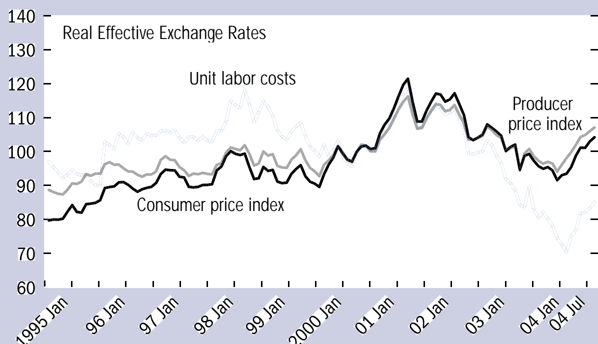
Moderate average movements in real effective exchange rates, however, mask a number of bumps in the road since the mid-1990s (Chart 1). During 1995–2001, Poland experienced a sizable real appreciation across all measures of competitiveness, and this took a toll on exports, output, and employment.

Chart 1

A bumpy road

Real effective exchange rates vis-à-vis Poland's trading partners are rising again

(2000=100)



Data: UN, Comtrade database; and IMF, staff calculations. The classification of exports is based on Peneder (1999 and 2001).

Subsequently, wage moderation together with nominal depreciation restored lost competitiveness, but Poland saw this trend reversed in the second quarter of 2004 when the real effective exchange rate again began to appreciate.

Export growth and profitability

Poland's export performance since 1995 had followed a similarly uneven path, reflecting swings in competitiveness and external shocks. Robust real growth of exports in the mid-1990s confirmed adequate or even strong initial levels of competitiveness, but export growth took a hit in 1999 when the country's export markets in Russia and the Commonwealth of Independent States (CIS) collapsed and in 2001 when demand declined as a result of an economic slowdown in the European Union (EU).

Export growth has recovered since late 2002, as Poland's currency, the zloty, weakened against the euro and the consequent nominal effective exchange rate depreciation has helped improve competitiveness. Foreign direct investment (FDI) inflows in the late 1990s also began to bear fruit. In response to all of these factors, Poland's export-to-GDP ratio has increased (albeit starting from a very low base) by 11 percentage points since 1993. While sizable, this increase has been substantially smaller than those recorded in some other central European countries, notably Hungary and Slovakia, which have seen their export ratios increase by 36 and 23 percentage points, respectively.

Not surprisingly, profitability has mirrored developments in competitiveness and overall export performance. Various measures of profitability suggest that Polish exporters squeezed profit margins during the periods of deteriorating competitiveness in an attempt to preserve market shares. Since 2002, export profitability has strengthened considerably, benefiting from both the industrial restructuring in the late 1990s and the depreciation of the zloty through early 2004. Overall, the export sector has been a driving force of economic growth in the past few years.

Poland has succeeded in expanding its market share in the EU. While it has not kept pace with some other central European countries and China, it has outperformed most non-European competitors. Poland has made little progress, however, in expanding its share in other major markets, such as the United States. These patterns may reflect, at least in part, factors other than changes in competitiveness. The rapid increase in China's export share, for example, may also be due to Asia's growing "vertical integration in production"—that is, components made, for example, in Southeast Asia but assembled in China and considered Chinese exports. And Poland's present edge over non-European competitors, such as Mexico, may

reflect the benefits of free trade agreements that it was able to enter into with the EU in the early and mid-1990s. Non-European competitors have since entered into similar EU arrangements but have not yet fully realized their benefits.

Product changes and labor shedding

Poland's export sector has had to adapt to remain profitable. Underlying structural changes in the economy, compounded by external factors, have significantly changed the product composition of exports. Like other transition economies, Poland in the early 1990s inherited a large industrial sector and an underdeveloped service sector. Its past participation in the Council for Mutual Economic Assistance (CMEA) heavily influenced Poland's export composition. As a CMEA member, it chiefly provided manufactured goods to the CIS in exchange for raw materials. With liberalization, the share of industry in output and employment declined, with ramifications for the export potential of different sectors. The permanent loss of export markets in the CIS countries following the 1998 Russia crisis exacerbated these underlying trends. Poland subsequently and successfully reoriented its exports toward EU markets, but this has necessitated demand-driven changes in the product structure of exports.

FDI inflows, too, have been instrumental in altering the product structure of Poland's exports. In the beginning of the transition period, much of the country's existing stock of capital was not up to the task of expanding exports to advanced countries. Subsequently, FDI inflows—for acquiring privatized existing firms and setting up new operations—have played a crucial role in upgrading technology, improving organizational capacity and product quality, expanding new production, and creating export capacities. The impact of FDI on export composition is evident at the sectoral level. Poland's machinery and transport equipment sector, which received the largest share (one-fourth) of FDI in manufacturing between 1993 and 2003, also recorded the largest increase in the share in total exports.

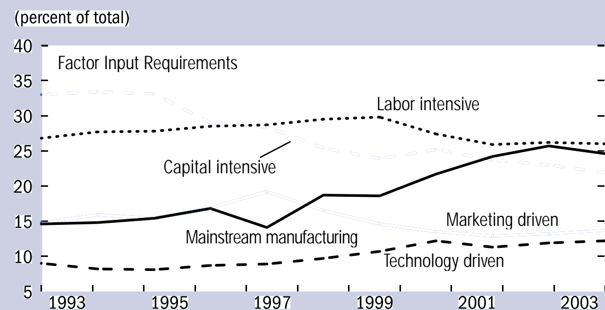
The changing product structure of exports has had implications for inputs, notably for capital, employment, and labor-skill levels. While the share of capital-intensive exports in total exports has declined quite rapidly, the share of labor-intensive exports remained broadly stable through 1999 but diminished thereafter (Chart 2). The share of mainstream manufacturing exports has increased rapidly since 1998, while the share of technology-driven exports has increased only slightly. Similarly, the labor-skill requirements of exports have also changed dramatically. The most striking result is the sharp fall, since 1993, in the share of exports requiring low-skill labor and the increase in the share of medium-skill labor-intensive exports. The low and stable share of high-skill labor exports appears consistent with the modest increase in the share of technology-driven exports.

Chart 2

Export composition is changing

The structure of Poland's exports is increasingly converging to that of advanced countries

(percent of total)



Data: IMF, Information Notice System, *International Financial Statistics*, and staff calculations; and UN, Common Database and Comtrade.

Unit labor costs in labor-intensive and low-skill industries rose faster than in other sectors between 1999 and 2003. It is likely that the increased costs contributed to the weakening competitiveness and poor export performance of these industries. Producers responded by shedding workers in an attempt to limit rising labor costs. This process was exacerbated by a minimum wage that constrained downward wage movements. Skill mismatches, in turn, may have hindered the absorption of the unemployed in higher productivity sectors. Beginning in 1999, Poland saw the falling share of labor-intensive and low-skill exports contribute to a rapid economywide decline in employment. By 2003, employment in export-oriented firms had decreased by 31 percent compared with a 13 percent increase in nonexporting firms.

Challenges for policymakers

While non-export sectors have taken up some of Poland's displaced workers, particularly in the past one to two years, the reabsorption has not been complete. Unemployment remains high at almost 19 percent. While this may reflect temporary frictions in the transition, it is likely that skill mismatches and insufficient wage flexibility have contributed. In this environment, it will be important to provide adequate training and to minimize labor market rigidities. With estimates of structural unemployment of about 15 percent, visible improvement may, however, be gradual. ■

Zuzana Murgasova
IMF European Department

Copies of *Republic of Poland: Selected Issues*, IMF, Country Report No. 04/218, are available for $15.00 each. See page 32 for ordering information.

The Eastern Caribbean region at a crossroads

Since 1990, the island states of the Eastern Caribbean Currency Union (ECCU) have seen their incomes grow at under 3 percent a year, less than half the rate of income growth in the 1980s. In recent years, sluggish growth has been compounded by rising indebtedness. What can be done to reinvigorate growth and address the region's high debt? A seminar—organized in Washington, D.C., in December 2004 by the Eastern Caribbean Central Bank (ECCB) and the IMF's Western Hemisphere Department—examined possible steps.

"The ECCU countries face a particular dilemma," said Sir K. Dwight Venner, Governor of the ECCB, in his opening address. Their populace expects high living standards because of the demonstration effect that is exerted by North American tourism and migration. And the "liberal democratic political system puts considerable pressure on incumbent governments to meet these expectations and on opposition parties to promise to exceed whatever governments are doing."

Venner pointed to the region's currency union—the EC dollar has been pegged to the U.S. dollar since 1976—as one factor that has helped the region's macroeconomic performance. The currency union has produced, he said, "a low rate of inflation as well as the confidence and credibility needed to support investment and economic growth."

Venner: Global economic forces can often be as implacable as the forces of nature.

At the same time, Venner said, the ability to provide strong income growth is constrained on the supply side. These are small countries, with small populations and few natural resources. They are also situated in a region subject to frequent natural disasters. In fact, according to a recent study by the IMF's Tobias Rasmussen, this is the most disaster-prone region in the world. Smallness also puts these countries at the mercy of global economic forces, Venner said, which can often be as implacable as the forces of nature. These island economies are quick to feel the effects of higher energy prices, rising global interest rates, global security concerns that dampen tourism, and the erosion of trade preferences in developed country markets.

Some of these size-related concerns, suggested Ratna Sahay, who leads the IMF's regional surveillance missions to the ECCU countries, could be addressed through further regional cooperation and integration. Such steps could expand small national markets by promoting greater mobility of labor, capital, and goods, and by helping to economize on fiscal resources through the collective provision of some government services.

Currency union: a "high maintenance" choice

While pointing to the ECCU's track record of macroeconomic stability, IMF Deputy Managing Director Agustín Carstens cautioned, however, that currency union was a "high maintenance" choice. Preserving a fixed exchange rate requires fiscal discipline, flexible factor markets, and a strong financial system, but in recent years, he noted, debt has risen rapidly in most ECCU countries and has now reached very high levels.

In four countries—Antigua & Barbuda, Dominica, Grenada, and St. Kitts & Nevis—the debt-to-GDP ratio has almost doubled since 1998 and outstanding public debt now exceeds the countries' annual income. David O. Robinson, IMF's mission chief to Antigua & Barbuda and St. Kitts & Nevis, highlighted the different paths these two countries took to debt buildup. In St. Kitts & Nevis, policy slippages—especially the failure to address the loss-making state-owned sugar industry—were exacerbated by three recent natural disasters. For Antigua and Barbuda, indebtedness followed years of fiscal profligacy and a lack of transparency. In Grenada, debt problems had their roots in a government decision to assume private debt that was then compounded by the effects of Hurricane Ivan in September 2004, according to Prakash Loungani, the IMF mission chief for the country. Dominica's experience offers a striking contrast. Alejandro Santos and Sanjaya Panth, two successive IMF mission chiefs to the country, documented how decisive actions by the authorities, taken in the context of an IMF-supported economic program from December 2003, quickly produced a virtuous circle of increased investor confidence, faster growth, and improved fiscal positions.

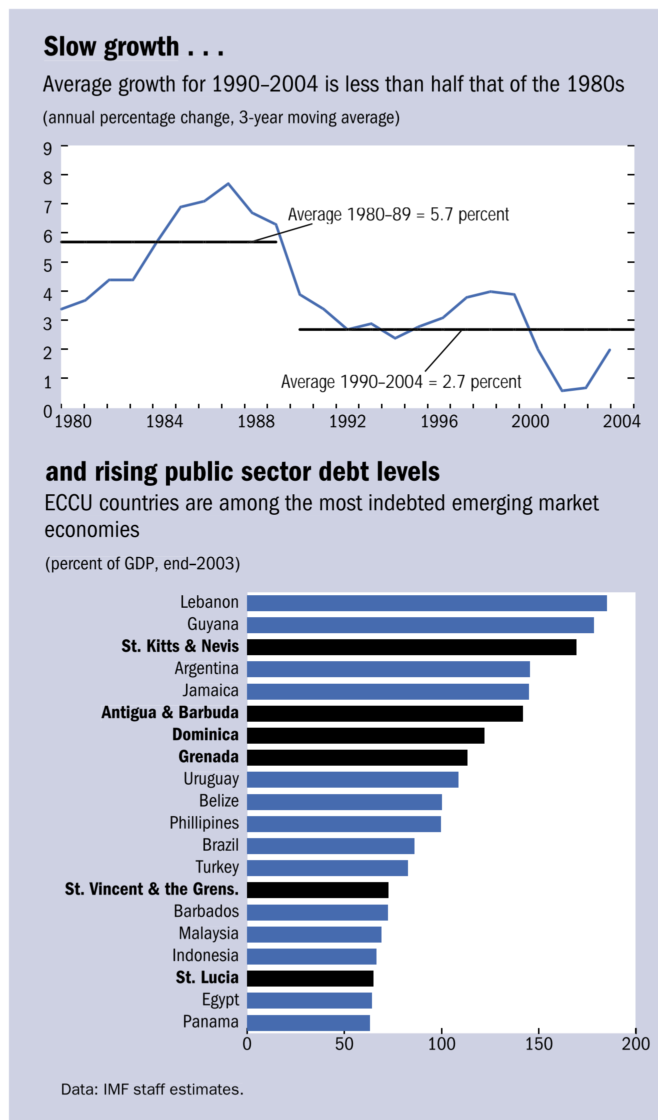
Dealing with debt

Achieving a sustainable debt burden, said Matthew Fisher, a Senior Advisor in the IMF's Policy Development and Review Department, requires a comprehensive macroeconomic framework that combines fiscal measures, growth-promoting structural reforms, asset mobilization, and international donor support. "There should be no illusion that restructuring provides

an easy way out.," Fisher said. Debt restructuring—currently under way in Dominica and being considered in Grenada following Hurricane Ivan—should always be used as a last resort and only as part of a comprehensive and credible macroeconomic strategy.

In this context, Sean Hagan, Director of the IMF's Legal Department, and Carlos Medeiros, Division Chief in the IMF's International Capital Markets Department, noted that countries considering debt restructuring would benefit from pursuing a preemptive and collaborative agreement with creditors to help restore confidence quickly and limit spillovers to the real and financial sectors of the economy. A key part of the debt-restructuring strategy is to ensure the viability of the domestic financial system following a debt restructuring, emphasized David Hoelscher, a Division Chief in the IMF's Monetary and Financial Systems Department.

Wendell Lawrence, Financial Secretary for St. Kitts & Nevis—one of the 12 officials from the ECCU region who participated in the seminar—welcomed the IMF staff's presentations as a good checklist of what to do and what to avoid for a country considering debt restructuring. Carstens underscored the IMF's willingness to work closely with the ECCU countries to restore debt sustainability, a message reinforced by the IMF's Executive Director Kevin Lynch, whose constituency includes the ECCU region, and by Anoop Singh, Director of the IMF's Western Hemisphere Department.



Fiscal adjustment can help

Creditors are more likely to agree to a restructuring if they are convinced that the country is taking strong fiscal measures to prevent a recurrence of the debt buildup. Are large fiscal adjustments viable options for the ECCU states to reduce their debt? Mark Flanagan, an Economist in the IMF's Fiscal Affairs Department, examined the experiences of 165 countries during 1971–2001. He found that many countries undertook large fiscal adjustments during this period and that the relatively more enduring episodes were marked by recurrent expenditure restraint and were set against a background of relative political stability. In general, such adjustments did not lead to even a short-term decline in growth.

Large fiscal adjustments are thus possible in the ECCU countries and are indeed being undertaken—in Dominica, for instance. But their success depends on winning public support for them. Formulating economic policy in a transparent manner, for instance through town-hall meetings with the public, could help build support for difficult reforms. Venner said that such outreach was essential to preserve one of the strengths of the ECCU member states, their "liberal democratic systems and respect for citizens' rights of expression."

Four IMF Executive Directors participated in the seminar: Lynch; Pier Carlo Padoan, whose constituency includes Italy; Moises Schwartz, whose constituency includes Mexico; and Nancy Jacklin, who represents the United States. Lynch lauded the IMF's efforts "on behalf of some of its smallest members," adding that these efforts "provide a concrete example of its genuine commitment to improving growth prospects and living standards across its entire membership." Venner concluded that the seminar reinforced an ongoing "process of engagement that begins with stabilization and the challenge of the debt overhang and moves to the matter of achieving sustainable development" of the ECCU countries. ■

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Morris Goldstein on China's currency policies

Renminbi appreciation seen in China's own best interest

Is China's currency significantly undervalued? Has China been manipulating its value contrary to IMF rules? Would an appreciation be in the interest of China and of the world economy? And what kind of currency policy action would be best? During a recent IMF Institute seminar, Morris Goldstein, Senior Fellow with the Institute for International Economics (IIE), proposed answers to these questions, drawing on his work with IIE colleague Nicholas Lardy.

Is the renminbi out of line? There are various ways to try to answer this question, Goldstein said, focusing on two: the "underlying balance" approach—which asks what exchange rate would produce equilibrium in a country's overall balance of payments after adjustments for the cyclical position of the economy and for lagged effects of recent exchange rate movements—and the "global payments imbalance" approach, which looks at how the currency fits into the broader adjustment of global payments imbalances, particularly the U.S. current account deficit.

Michael Spilotro/IMF

Goldstein: "You cannot find a better candidate for appreciation than China."

Applying the first approach, Goldstein estimated "normal" net capital inflows of 1½ percent of GDP. He did this by looking at China's capital account over the past decade, assuming that China's controls on capital flows would be broadly maintained, and leaving aside exceptional periods like 2003 and 2004 when there had been large speculative capital inflows driven by (unrealized) expectations that the renminbi would appreciate. China's current account has also shown an underlying surplus in recent years. In 2003, the underlying surplus on the current account was equivalent to around 4½ percent of GDP by Goldstein's estimate, although the actual surplus was smaller owing to the overheating economy, which had driven up import demand, and because positive trade effects had not yet materialized from the renminbi's real effective deprecation since 2002. But China would have needed an average current account deficit of around 1½ percent of GDP to offset its normal net capital inflow. There was thus a roughly 6 percent of GDP difference between the underlying current account balance and the amount needed to offset normal capital flows. Using estimates of the sensitivity of trade flows to exchange rate changes, this meant that the renminbi would have to appreciate by 25–35 percent to restore equilibrium to China's overall balance of payments. Goldstein noted that preliminary data for the first three quarters of 2004 suggested a somewhat smaller estimate for China's underlying current account surplus, which would imply that a 15–30 percent appreciation of the renminbi would be needed to restore equilibrium.

Why would such a sizable appreciation be needed to reduce China's trade balance? A key reason, he explained, is that China, as a regional processing center, imports a large volume of inputs for assembly and export. The high import content of China's exports, at about 35–40 percent, means that there is less of an export increase from a currency appreciation than there would be otherwise, so a bigger exchange rate change would be needed to change the trade balance.

Using the global payments imbalance approach and assuming a sustainable current account deficit for the United States of around 2½ percent of GDP—compared with the 2004 deficit of 5½ percent of GDP—Goldstein estimated that a real depreciation of 30–35 percent from the dollar's peak in early 2002 would be required. With the dollar now having fallen by around 15–20 percent from its peak, how should the needed improvement in the U.S. current account and implied further appreciation of other currencies be shared internationally?

Distinguishing surplus countries from deficit countries, considering countries' differing abilities to shift demand from external to domestic sources, and taking account of other relevant factors such as the extent of recent exchange rate adjustments and countries' reserve holdings, Goldstein concluded that "you cannot find a better candidate for appreciation than China."

A classic remedy

Recalling the work of Nobel prize–winning economist James Meade, Goldstein argued that exchange rate appreciation is a classic remedy for an economy, such as China's, that has a large external surplus, more than ample reserves, and domestic overheating. Contrasting China (which has a weight of some 10 percent in the U.S. Federal Reserve's broad index for the dollar) with the euro area (which has an index weight of about 18 percent, a current account surplus of less than 1 per-

cent of GDP, and a growth rate of 2 percent or less), he pointed out that since the dollar's peak in 2002, in real trade-weighted terms, the renminbi had depreciated by about 10 percent while the euro had appreciated by over 20 percent.

China is not the only country for which a case can be made for currency appreciation, he emphasized, noting that China's 10 percent weight in the dollar index means that a broader-based dollar depreciation would be needed to significantly cut the U.S. current account deficit. But although a renminbi appreciation by itself would not have a big impact, such a step could prompt appreciations vis-à-vis the dollar of other Asian currencies that were also undervalued.

This global payments analysis, Goldstein maintained, also yields the conclusion that the renminbi is undervalued by at least 15–20 percent. "I am not saying that the preferred approach to bringing global payments imbalances into adjustment is by exchange rate changes alone," Goldstein said, acknowledging that adjustments of domestic saving-investment imbalances were also needed.

A call for stronger IMF surveillance

Has China been manipulating the renminbi's value? Goldstein harked back to the competitive devaluations of the 1920s and 1930s, which convinced the international community to draw up international rules to discourage "beggar-thy-neighbor policies" and provided a main motive for establishing the IMF. Pointing out that the principles of IMF surveillance over exchange rate policies adopted in 1977 specifically cited "protracted, large-scale intervention in one direction in the exchange market" as a development that should prompt the IMF to discuss exchange rate policies with the member country, he argued there is, by this criterion, "prima facie evidence of manipulation," given "the huge, steady increase" in China's reserves over the past two years.

"If there is a perception that no one is minding the store at the international level, these concerns about manipulation don't go away; they are handled much less well at the bilateral level," he warned. "This debate would be handled much better in the IMF, which is the place to do it!" he added, while conceding that the verdict might differ from his own.

Goldstein dismissed the argument that there can be no charge of manipulation because a country is free under the IMF's Articles of Agreement to opt for the currency regime of its own choice. While a country does have the right to intervene in exchange markets, he said, no country should try to maintain the "wrong" rate by engaging in "protracted, large-scale intervention in one direction in the exchange market." He was also unpersuaded by the idea that manipulation cannot occur if a country keeps the same currency peg over a long period of time. (China has kept its exchange rate fixed at RMB8.28 to the dollar since 1995.) Misalignment of the real exchange rate, he pointed out, can also occur from nonmovement of the nominal exchange rate against the backdrop of a balance of payments surplus and a depreciating real exchange rate.

Appreciation for China's sake

Would an increase in the renminbi's value be in China's own interest and that of the rest of the world? Goldstein responded without hesitation, "yes and yes." From China's perspective, the critical question, he said, is whether the current level of exchange rate helps the country achieve its economic policy goals, such as high and sustainable growth, low inflation, banking reform, and continued secure market access for exports. Clearly, it doesn't, he insisted.

The undervalued renminbi, he explained, has been linked to excessive credit growth and overheating because it attracts large capital inflows motivated by expectations of appreciation and because of the associated accumulation of reserves. He also warned that a significantly undervalued renminbi could incite protectionist pressures in the United States and Europe, causing China to lose some of its market access. Moreover, he disputed the view that appreciation is the main threat to China's growth and employment, noting that an unsustainable credit boom—which could require drastic administrative controls or interest rate hikes—and protectionist actions against exports pose the most serious threat to growth.

As for the rest of the world, the undervalued renminbi makes it more difficult to reduce global payments imbalances. If the Chinese economy has a hard landing brought on by the undervalued rate, there would be additional negative repercussions. And those hit, Goldstein observed, would not be limited to East Asia, considering China's strong demand in recent years for primary commodities.

Two-stage policy solution

So how should China tackle the alleged problem with the renminbi's value? Goldstein dismissed three options. A "go slow" approach—using a series of trade, capital account, and tax measures to substitute for a medium-sized revaluation, perhaps together with a small revaluation (say, of no more than 3 percent)—might seem appealing because it would likely have only minor effects on China's exports and growth. But it would not solve the problem of large capital inflows and would likely fuel expectations of a larger revaluation later. Another option is for China to move rapidly to open its capital markets and float its currency. "This is a good idea for the long run but a bad idea for now," said Goldstein, since China's currently weak banking sys-

tem is susceptible to large-scale freed-up capital flight and high exchange rate volatility. A third option—delinking the capital account from the exchange rate by keeping controls on capital outflows and simultaneously introducing a managed floating system—would, Goldstein expected, result in "plenty of 'management' and very little 'floating' in China's case." A heavily managed float would fail to remove the existing disequilibrium and would end up resembling the "go slow" approach.

A "two-stage" currency reform would be better and would provide a solution to China's particular policy dilemma, Goldstein concluded. As a first stage, he recommended that China revalue the renminbi by 15–20 percent and at the same time switch its peg from the dollar to a basket of currencies and widen the margins around the new parity to 5–7 percent (from less than 1 percent now), while maintaining restrictions on capital outflows. During a second stage—down the road once China's banking system strengthens—China should adopt a managed float and significantly liberalize controls on capital outflows.

This two-stage option would remove the incentive for further large capital inflows by sufficiently revaluing the currency. Repegging to a currency basket would give greater stability to the overall effective rate than with the unilateral dollar peg, and greater exchange rate flexibility at a later stage would give China the monetary independence it needs. Exchange rate policy would become the ally, rather than the enemy, of bank reform. The rest of the world would not have to live with a significantly undervalued renminbi, while China would be promoting the right sequencing of reforms. ■

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IMF External Relations Department

For more information, see Morris Goldstein's recent paper, "Adjusting China's Exchange Rate Policies," at http://www.iie.com/publications/publications.htm

China: Getting sequencing of liberalization right

In the tricky matter of sequencing exchange rate flexibility and capital account liberalization, which is the cart and which is the horse? A recently released IMF Policy Discussion Paper (No. 05/1) argues that for China, a more flexible exchange rate regime is the higher priority and in its own interest. Greater flexibility would allow China to operate a more independent monetary policy, which would provide a useful buffer against domestic and external shocks. Greater exchange rate flexibility and steps to ensure a more stable and robust financial system would then put China in a position to pursue substantial capital account liberalization, say authors Eswar Prasad, Thomas Rumbaugh, and Qing Wang.

But does a move toward exchange rate flexibility necessarily involve a revaluation? Estimating equilibrium exchange rates is a difficult endeavor, especially for a developing economy like China that is undergoing substantial structural change. Indeed, analyses by IMF staff show that existing techniques provide a wide range of estimates of the equilibrium value of the renminbi, with a substantial degree of uncertainty associated with each of those estimates.

Many observers have interpreted the recent surge in reserve accumulation as clear evidence of the renminbi's undervaluation. However, the increase in reserves appears to have been significantly influenced by inflows of speculative capital, suggesting that the evidence on whether the renminbi is substantially undervalued in terms of fundamentals is far from conclusive. The medium-term trend in the real exchange rate, the authors observe, is even harder to predict as it will depend on a variety of factors with potentially offsetting effects.

Thus, although the renminbi might be expected to appreciate initially with a move toward more flexibility, there is no obvious reason why such a move should involve a significant revaluation. The paper also sees no need to move to the immediate adoption of a free float. It notes that an initial move toward flexibility could take the form of a widening of the renminbi trading band, a peg to a currency basket, or some combination of these. With capital controls in place, greater exchange rate flexibility seems unlikely to subject China's banking system to substantial stress, although the weaknesses in the system argue for taking a cautious and gradual approach to capital account liberalization.

Capital controls tend, of course, to have their effectiveness eroded over time, which could make a phased move toward flexibility increasingly complicated as time passes. And the experiences of other countries clearly show the merits of making a move toward flexibility when the domestic economy is growing rapidly and the country's external position is strong. All of this suggests that a relatively early move toward greater exchange rate flexibility would be in China's best interest. ■

Copies of IMF Policy Discussion Paper No. 05/1, *Putting the Cart Before the Horse? Capital Account Liberalization and Exchange Rate Flexibility in China*, are available for $15.00 each from IMF Publication Services. See page 32 for ordering details. The full text is also available on the IMF's website (*www.imf.org*).

HIPC debt relief (status as of January 27, 2005)

IMF member	Decision point	Completion point	Amount committed	Amount disbursed[1]
			(million SDRs)	
Heavily Indebted Poor Countries (HIPC) Initiative				
Under original 1996 initiative				
Bolivia	September 1997	September 1998	21.2	21.2
Burkina Faso	September 1997	July 2000	16.3	16.3
Côte d'Ivoire	March 1998	--	16.7[2]	--
Guyana	December 1997	May 1999	25.6	25.6
Mali	September 1998	September 2000	10.8	10.8
Mozambique	April 1998	June 1999	93.2	93.2
Uganda	April 1997	April 1998	51.5	51.5
Total original HIPC			**235.3**	**218.6**
Under the Enhanced HIPC Initiative				
Benin	July 2000	March 2003	18.4	20.1
Bolivia	February 2000	June 2001	41.1	44.2
Burkina Faso	July 2000	April 2002	27.7	29.7
Cameroon	October 2000	Floating	28.5	5.5
Chad	May 2001	Floating	14.3	7.2
Congo, Democratic Republic of	July 2003	Floating	228.3[3]	2.3
Ethiopia	November 2001	April 2004	26.9[4]	28.1
Gambia, The	December 2000	Floating	1.8	0.1
Ghana	February 2002	July 2004	90.1	94.3
Guinea	December 2000	Floating	24.2	5.2
Guinea-Bissau	December 2000	Floating	9.2	0.5
Guyana	November 2000	December 2003	31.1	34.0
Honduras	June 2000	Floating	22.7	8.8
Madagascar	December 2000	October 2004	14.7	16.4
Malawi	December 2000	Floating	23.1	6.9
Mali	September 2000	March 2003	34.7	38.5
Mauritania	February 2000	June 2002	34.8	38.4
Mozambique	April 2000	September 2001	13.7	14.8
Nicaragua	December 2000	January 2004	63.5	71.2
Niger	December 2000	April 2004	21.6[5]	24.1
Rwanda	December 2000	Floating	33.8	14.4
São Tomé and Princípe	December 2000	Floating	--	--
Senegal	June 2000	April 2004	33.8	38.4
Sierra Leone	March 2002	Floating	98.5	62.0
Tanzania	April 2000	November 2001	89.0	96.4
Uganda	February 2000	May 2000	68.1	70.2
Zambia	December 2000	Floating	468.8	351.6
Total Enhanced HIPC			**1,562.4**	**1,123.4**
Combined total for 28 members			**1,797.7**	**1,342.0**

Definitions

Decision Point: Point at which the IMF decides whether a member qualifies for assistance under the HIPC Initiative (normally at the end of the initial three-year performance period) and decides on the amount of assistance to be committed.

Completion Point: Point at which the country receives the bulk of its assistance under the HIPC Initiative, without any further policy conditions. Under the enhanced HIPC Initiative, the timing of the completion point is linked to the implementation of pre-agreed key structural reforms (that is, floating completion point).

[1] Includes interest on amounts committed under the Enhanced HIPC Initiative.

[2] Equivalent to the committed amount of $22.5 million at decision point exchange rates for March 17, 1998.

[3] Amount committed is equivalent to the remaining balance of the total IMF HIPC assistance of SDR 337.9 million, after deducting SDR 109.6 million representing the concessional element associated with the disbursement of a loan under the Poverty Reduction and Growth Facility following the Democratic Republic of the Congo's clearance of arrears to the IMF on June 12, 2002.

[4] Excludes commitment of additional enhanced HIPC assistance of SDR 18.19 million subject to receipt of satisfactory financing assurances from other creditors.

[5] Excludes commitment of additional enhanced HIPC assistance of SDR 9.664 million subject to receipt of satisfactory financing assurances from other creditors.

Data: IMF Finance Department.

IMF stresses commitment to help fight HIV/AIDS

The IMF has been battling perceptions that it is holding back critical health spending—including on HIV/AIDS—in countries with IMF-supported adjustment programs. To increase awareness about its approach, the IMF's Fiscal Affairs Department invited donors, international agencies, and nongovernmental organizations (NGOs) to discuss the issue on January 19.

This workshop, a follow-up to one last year (*IMF Survey*, July 12, 2004), focused on problems experienced in boosting aid to four countries: Honduras, Kenya, Uganda, and Zambia. Participants told IMF mission chiefs for these countries—all of which have economic programs supported by the IMF's Poverty Reduction and Growth Facility—about problems ranging from a lack of health care professionals (for instance, graduating nurses in Zambia account for just 2 percent of all nurses, while graduating teachers represent almost 10 percent of all teachers) to inadequate treatment facilities and an unreliable supply of drugs and other medical supplies. Countries were also sometimes reluctant to increase spending on HIV/ AIDS, pointing to the need to comply with fiscal ceilings in IMF programs.

IMF staff told participants that IMF-supported programs usually contain a ceiling on net credit to governments designed to help countries achieve fiscal stability, which is essential for economic growth. Each country then decides on specific spending priorities, and IMF-supported programs do not specify hard budget ceilings on health care spending. If more money becomes available for critical social programs, especially in the form of grants, the IMF will help the country revise its spending plans.

IMF staff also said that countries need help to develop their capacity to absorb larger amounts of aid. While money might be flowing into the country, this doesn't help if there aren't enough trained nurses and other health workers.

Another issue is that aid flows are unpredictable, which often makes it difficult for countries to manage their budgets from one year to the next and makes them wary about making long-term commitments. For instance, many governments are reluctant to hire more health workers without donor assurances of continued financing. Kenya eliminated school fees as part of a program to achieve universal primary education, only to experience a sharp reduction in aid flows that then forced the government to reallocate scarce domestic revenues to the education sector.

Workshop participants pointed out that they deal mainly with health ministries, while IMF staff typically work with finance ministry officials. Participants suggested that discussions about budget priorities in the health sector include as many stakeholders as possible, not least the ministry of finance. Greater clarity is needed on the factors determining the sectoral spending priorities of ministries of finance and on the impact of fiscal ceilings set in the context of IMF programs.

Participants also said the IMF needs to do more to clarify its role. Because most IMF country reports do not explicitly discuss the health sector, they give the impression that the IMF has not considered the need to ensure fiscal space for health spending. Participants suggested that the IMF work with donors and NGOs to clarify how fiscal ceilings are decided. The IMF should also reassure governments that program ceilings are flexible and can accommodate additional spending if new financing becomes available, as long as it is compatible with fiscal and debt sustainability. ■

Who attended?

The workshop included representatives from a wide variety of agencies involved in HIV/AIDS work, including policy research institutes (Center for Global Development, Fogarty Center of the National Institutes of Health, and The Futures Group); nongovernmental organizations (NGOs) (Catholic Relief Agencies, DATA, the Global Fight, and Project Hope); the Global Fund to Fight AIDS, Tuberculosis, and Malaria; and UNAIDS and World Health Organization; as well as developing countries (staff from the IMF Executive Directors' offices for the African constituencies); donor countries (Belgium, European Commission, staff from IMF Executive Directors' offices for the Nordic countries); the U.S. government's Presidential Emergency Plan for AIDS Relief; and the World Bank.

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