January 2003
Corrected: January 2003*
IMF Country Report No. 03/06

Madagascar: 2002 Article IV Consultation, Second Review Under the Poverty Reduction and Growth Facility, and Requests for Extension of Arrangement, Waiver of Performance Criteria, and Additional Interim Assistance Under the Enhanced Initiative for Heavily Indebted Poor Countries—Staff Report; and Public Information Notice and News Brief on the Executive Board Discussion

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of a combined discussion of the 2002 Article IV consultation with **Madagascar** and the second review under the Poverty Reduction and Growth Facility, and requests for extension of arrangement, waiver of performance criteria, and additional interim assistance under the enhanced Initiative for Heavily Indebted Poor Countries, the following documents have been released and are included in this package:

- the staff report for the 2002 Article IV consultation and the Second Review Under the Poverty Reduction and Growth Facility, and Requests for Extension of Arrangement, Waiver of Performance Criteria, and Additional Interim Assistance Under the Enhanced Initiative for Heavily Indebted Poor Countries, prepared by a staff team of the IMF, following discussions that ended on **November 13, 2002**, with the officials of Madagascar on economic developments and policies. **Based on information available at the time of these discussions, the staff report was completed on December 6, 2002**. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF; and

- A Public Information Notice (PIN) and a News Brief summarizing the **views of the Executive Board as expressed during the December 23, 2002 discussion** of the staff report on issues related to the Article IV consultation and the IMF arrangement, respectively.

The document(s) listed below have been or will be separately released.

Joint Staff Assessment of the Poverty Reduction Strategy Paper Progress Report
Poverty Reduction Strategy Paper—Progress Report
Letter of Intent sent to the IMF by the authorities of Madagascar**
Memorandum of Economic and Financial Policies by the authorities of Madagascar**
Technical Memorandum of Understanding**
Selected Issues Paper and Statistical Appendix

*Table 9 revised
**May also be included in Staff Report

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International Monetary Fund
Washington, D.C.

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MADAGASCAR

Staff Report for the 2002 Article IV Consultation, Second Review Under the Poverty Reduction and Growth Facility, and Requests for Extension of Arrangement, Waiver of Performance Criteria, and for Interim Assistance under the Enhanced Initiative for Heavily Indebted Poor Countries

Prepared by African Department

(In consultation with the Fiscal Affairs, Legal, Policy Development and Review, Statistics, and Treasurer's Departments)

Approved by José Fajgenbaum and Martin Fetherston

December 6, 2002

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- Macroeconomic developments under the PRGF-supported program in 2001 were encouraging, broadly meeting or exceeding program targets, with the exception of tax revenue. Real GDP rose by 6 percent, and the rate of inflation declined to 4.8 percent during 2001. Exports rose by 21 percent in SDR terms, spurred by the expansion of export processing zone production. As a result, the external current account deficit declined to 1.3 percent, less than programmed, and the increase in international reserves exceeded the program's target.

- Fiscal performance was satisfactory in the first half of 2001, but revenues in the second half fell short of target, largely because of weakness in customs administration. Progress was made in strengthening budgetary management and treasury accounting. The tender for the telecommunications company was completed, but the negotiation with the buyer is still pending.

- The political crisis in the first half of 2002, following the December 2001 presidential election, led to a split of the country between the two contenders. The extensive blockades of roads brought industrial production almost to a halt, with a severe effect on incomes and a sharp rise in poverty, and hampered the marketing of agricultural products. Foreign exchange operations were disrupted, as the central bank branch network came under two different managements and the external reserves were frozen. Following a recount of the vote in early May, Mr. Ravalomanana was inaugurated as President; in early July, the crisis was resolved with the departure of the incumbent President Ratsiraka.

- The recovery of industrial production so far in 2002 has been only gradual, as foreign orders for the textile industry were lost. Real GDP is projected to fall by 12 percent in 2002. Prices shot up in the first five months of the year and then started to decline. Government revenue collection was very low in the first half of the year, and a large number of investment projects were suspended.

- Beginning in July the new government has adopted a number of measures to promote recovery of the private sector, and to alleviate the impact of the crisis on the most vulnerable groups. With the resumption of donor support, the government was able to start repaying arrears to the private sector, assisting in their recovery. At the reopening of the foreign exchange market in August, the currency depreciated by 11 percent in nominal effective terms and has remained broadly stable since then.

Policies for 2003

- The new government aims at fostering growth and reducing poverty through a rapid implementation of public the investment program, mostly foreign financed, and creating a climate favorable to private investment. To that end it is determined to improve governance at all levels, and to fight corruption vigorously.

- In 2003 real GDP is expected to grow by 8 percent, as economic activity recovers from its low level and foreign-financed public investment increases sharply. The external current account deficit is projected to widen, but gross official reserves are projected to increase.

- The 2003 budget is predicated on a recovery of tax collection to 10.5 percent of GDP; the custom duties on inputs for the textile, agriculture, and construction sectors were reduced in early November, and the maximum tariff rate cut from 30 to 25 percent. The VAT refund system for the export processing zone will be revamped, and the VAT system on imported capital goods will be revised. The HIPC Initiative expenditure tracking will be strengthened. Treasury and budgetary management will be reinforced, to improve transparency

- Public enterprises will be privatized or restructured to facilitate their future privatization. Air Madagascar has been placed under a foreign management contract, and the capital of the cotton company, HASYMA, will be opened shortly to further private participation. The railroads have been put under concession with a company with foreign majority participation.

- The PRSP will be finalized in early 2003. It will give priority to good governance, and will emphasize rural development, an improved transportation network, and better social services. A PRSP progress status report and a joint staff assessment are issued jointly with this report.

Issues highlighted in the staff appraisal

- The budget for 2003 is consistent with the macroeconomic constraints, and places an appropriate emphasis on revenue mobilization and on wage restraint.

- The determination of the new government to increase transparency and improve governance at all level of public administration is welcome, and essential to promote a return of foreign investment. It is important that weaknesses in tax administration be corrected to increase revenue collection.

- Administrative procedures need to be streamlined to ensure faster expenditure commitment and execution of donor-funded projects. The tracking of poverty–related expenditures must be reinforced and accompanied by a monitoring of physical outcomes in the priority sectors.

I. Introduction

1. Discussions for the 2002 Article IV consultation and the second review under the three-year Poverty Reduction and Growth Facility (PRGF) arrangement for Madagascar were held during October 7-21 in Antananarivo and during November 11-13 at headquarters.[1] The second review under the PRGF-supported program, approved on March 1, 2001, was delayed due to the political crisis (see below). In the attached letter of transmittal and memorandum of economic and financial policies (MEFP) dated December 4, 2002 (Appendix I), the Minister of Economy, Finance, and Budget reviews progress made under the 2001 program, and outlines the government's economic recovery program and the policies to be implemented during the remainder of 2002 and in 2003. He also requests waivers for the nonobservance of end-December 2001 performance criteria (Appendix I, Table 1), and an extension of the PRGF arrangement from end-February 2004 to end-November 2004, as well as additional interim assistance under the enhanced Initiative for Heavily Indebted Poor Countries (HIPC Initiative) for the period January 1–December 31, 2003. The schedule of future disbursements and program reviews is presented in Table 1.

2. At end-September 2002, Madagascar's outstanding use of Fund resources amounted to the equivalent of SDR 100.02 million (81.85 percent of quota). Madagascar accepted the obligations of Article VIII, Sections 2(*a*), 3, and 4, effective September 18, 1996, and maintains no restrictions on the making of payments and transfers for current international transactions.

3. In concluding the 2001 Article IV consultation, on December 5, 2001, Executive Directors stressed the need to streamline administrative regulations, improve basic infrastructure, and continue to simplify and liberalize the trade regime in order to maintain Madagascar's attractiveness to foreign investors. They also expressed concern that the weak revenue performance in 2001 could have a negative impact on social and capital spending, and welcomed planned actions to strengthen tax and customs administrations, as well as taxpayer compliance. Directors welcomed the government's commitment to improve governance and the transparency of government operations, and encouraged the authorities to expeditiously complete the privatization program and the envisaged improvements of the regulatory framework and the judicial system.

4. The coordination of structural reform has been enhanced in the context of the HIPC Initiative and the preparation of the poverty reduction strategy paper (PRSP). A progress

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[1] The principal Malagasy representatives included Mr. Benjamin Radavidson, the Minister of Economy, Finance, and Budget, and Mr. Gaston Ravelojaona, Governor of the Central Bank of Madagascar. The mission also met with the Prime Minister, Mr. Sylla, and with the head of state, Mr. Ravalomanana. The staff representatives were Mr. Sacerdoti (Head), Messrs. Cady and Ould-Abdallah, Ms. Sancak (all AFR), Mr. Luzio (PDR), and Mrs. Afambo (Assistant-AFR). Mr. Dahl, the Fund Senior Resident Representative, participated in the work of the mission, which also worked closely with the World Bank staff.

report on PRSP preparation and a joint staff assessment are being issued jointly with this report. Structural reforms monitored under the PRGF-supported program focus on improving tax administration and budgetary management, which are essential for attaining the program's macroeconomic objectives; structural reforms in other areas are being supported by various donors and creditors (see Box 1). The World Bank is providing Madagascar with financial assistance through a US$100 million structural adjustment credit (SAC II), fully disbursed in October 2002, an Emergency Economic Recovery Credit (EERC) approved on November 14, 2002, and other credits, including for public sector management and private sector development. The European Union is also supporting Madagascar's adjustment efforts through a structural adjustment grant focusing on budgetary management and health sector reforms. Relations with the Fund and the World Bank Group are summarized in Appendices II and III, respectively.

5. Legislative elections are planned for December 15, 2002, and municipal elections will be held in 2003.

II. Recent Economic Developments and Performance Under the 2001 Program

6. After a period of instability in the early and mid-1990s, Madagascar made significant progress in terms of macroeconomic stabilization, structural reform, and poverty reduction in the late 1990s. Over the period, 1997-2000 the growth rate of real GDP averaged 4¼ percent, and the incidence of poverty was reduced from 73 percent to 69 percent of the population; meanwhile, inflation remained subdued. Exports doubled, spurred by the expansion of the export processing zone (EPZ), and international reserves rose sharply, reflecting also substantial foreign direct investment since 1999. Public finances strengthened, with government revenue rising from 8.7 percent of GDP in 1996 to 11.7 percent in 2000. An ambitious privatization program was initiated in 1998, leading to the privatization of the two state banks and the petroleum refinery and marketing company, SOLIMA, while the private sector strategy for other sectors was launched.

7. **Macroeconomic developments under the PRGF-supported program in 2001 were encouraging, broadly meeting or exceeding the program targets, with the exception of tax revenue.** Real GDP rose by 6 percent, permitting a further increase in real per capita GDP, while the rate of consumer price inflation on a year-on-year basis was reduced from 8.7 percent at end-2000 to 4.8 percent at end-2001 (Figure 1 and Table 2). Madagascar's textile and apparel exports benefited significantly from the U.S. African Growth and Opportunity Act (AGOA), while high international vanilla prices boosted traditional export earnings. As a result, the external current account deficit (including grants) declined much more than programmed, from 5.6 percent of GDP in 2000 to 1.3 percent in 2001 (Figure 2). Reflecting the improved current account, strong foreign direct investment, and external financing, mostly project related, net official reserves rose by SDR 77 million, exceeding program targets by a wide margin; the gross reserve coverage rose to the equivalent of 14.4 weeks' imports at end-2001 from 10.2 weeks of imports at end-2000.

Box 1. Structural Conditionality

Coverage of structural conditionality in the program for 2002-03

Structural performance criteria and benchmarks cover measures to strengthen tax administration, treasury accounting, budgetary audits, including audits of accounts of public enterprises, and the audit function in the central bank; these measures are essential to correct weaknesses in budgetary management, which can hamper macroeconomic controls, and to strengthen the safeguard system in the central bank.

Status of structural conditionality in earlier programs

Under the 2001 program supported by the PRGF arrangement, all measures covered by structural conditionality were implemented, except for the structural benchmark providing for the introduction of the more advanced version of the computerized customs information system, ASYCUDA (3 ++). This software system will now be put in place in early 2003; the delay is due to the late provision of technical assistance. The tender for the sale of the telecommunications company, TELMA, was launched, and the winner was selected in December 2001, complying with a benchmark under the 2000 program, which provided for the sale of either TELMA or Air Madagascar. For Air Madagascar, the government decided in mid-2002 to place the company under a management contract with a foreign airline management company, and the new management began operations in October. The World Bank staff is of the view that a delay in the privatization of Air Madagascar is appropriate in the present international economic environment.

Structural areas covered by World Bank and African Development Bank conditionality

The World Bank is providing assistance to structural reforms in areas relevant to the Fund-supported program through a second structural adjustment credit, a public sector management assistance credit, and an emergency economic recovery credit. Key actions supported by these credits in 2001-02 include (i) assistance in the completion of the privatization of TELMA; preparation of the strategy for the privatization of companies in the cotton and sugar sectors and assistance in strengthening the management of the electricity company, JIRAMA; (ii) reforms in the mining sector, including adoption of implementing decrees for the mining code and assistance to the mining land registry; (iii) reforms in the system of fishing licenses to achieve more transparency; (iv) strengthening of the judicial system, with assistance to the magistrates' training school, the publication of legal compendiums, the simplification of judicial procedures, and the reform of the business law; (v) assistance to the budget, treasury, and domestic tax administration with the provision of computer equipment and software, the design of more efficient administrative procedures, and the improved monitoring of tax collection; and (vi) assistance to the technical secretariat for the adjustment program, in particular for strengthening the monitoring of social expenditures.

The African Development Bank structural adjustment credit of 2001 included conditionality concerning the adoption of a new civil service statute, which was adopted by parliament at end-2001.

Structural measures covered by HIPC Initiative completion point conditionality

The floating completion point conditionality includes the following measures relevant to the PRGF-supported program: (i) the strengthening of the budgetary control systems through adoption of appropriate legislative changes, and increased staffing and resources of the state inspectorate general and of the budgetary control directorate; (ii) the implementation of a system for monitoring the expenditure process (commitment, payments order, and payment) for at least six ministries, including those of health and education; (iii) the improvement of the consolidation procedures for the balances of all the principal treasurers as a step toward the establishment of reliable opening and closing treasury balances; (iv) the preparation during 2001-02 of the budgetary execution law for 1999 and 2000; and (v) the preparation of biannual reports on education and health sector activities, including budgetary execution and physical achievements.

Other relevant structural conditions not included in current program

A desirable measure in the area of budgetary management is the adoption of a medium-term expenditure framework (MTEF). Initial steps toward the preparation of a MTEF are being taken in the context of the preparation of the PRSP. A more thorough plan toward the establishment of a MTEF will be defined in the second half of 2003.

8. During 2001, the Malagasy franc appreciated by about 7 percent in nominal effective terms and 9.6 percent in real effective terms, on the basis of relative CPI's (Figure 3), following a similar real appreciation in 2000. However, rising productivity offset part of the wage increases in 2000–01, so that the real effective appreciation measured on the basis of relative unit labor costs was much more modest over the two years, thereby maintaining the country's attractiveness to foreign direct investment. An analysis of trends in Madagascar's competitiveness is presented in the accompanying selected issues and statistical appendix paper.

9. **Fiscal performance in 2001 was satisfactory in the first half of the year, but revenue in the second half of the year fell substantially short of target, owing largely to weaknesses in the customs administration**. For the year, budgetary revenue reached 10 percent of GDP, compared with the revised program target of 11.9 percent (Tables 3, 4, and 5). Customs revenue in the second half of the year was considerably lower than in the first half, contrary to the normal seasonal trend. The deteriorating performance was attributable to the continuing disorganization of customs service at secondary ports, as well as to some exceptional exemptions granted in the run-up to the December 2001 presidential elections. Despite these revenue developments, the overall deficit, on a commitment basis and excluding grants, was contained at 8.1 percent of GDP, as against the 9.9 percent targeted, as government expenditures were 2.8 percent of GDP lower than programmed because of a shortfall in capital expenditure. Current expenditures were only marginally higher than targeted, as a shortfall in expenditures on goods and services, including those financed by HIPC Initiative debt relief, was offset by significant election-related overruns of expenditures through the special fund of the presidency (estimated at 0.6 percent of GDP). In mid-July 2002, the new government commissioned the State Inspectorate General to audit both the use of the presidential special fund in 2001 and of the HIPC Initiative-financed expenditure; while the latter showed that expenditures in the priority sectors were committed as planned, donors considered that some should have been better targeted, particularly in the rural roads area.

10. **External budgetary financing was about 1 percent of GDP lower than programmed,** as (i) the disbursement of the second tranche of the World Bank SAC II (US$30 million) was delayed until January 2002 because of the late selection of a winner of the tender for the telecommunications company, TELMA, and (ii) the disbursement of a tranche of the European Union structural adjustment assistance was postponed because of delays in the negotiations of conditionalities. With privatization receipts also lower than programmed by FMG 90 billion (0.3 percent of GDP), as proceeds of the sale of certain assets of the petroleum company were delayed to 2002, bank financing of the government exceeded the revised program by 0.7 percent of GDP.

11. In 2001, the decline in money velocity, which was associated with the significant profitability of the export sector and high investments, was stronger than originally programmed, so that money growth reached 24 percent, while inflation abated. With inflation declining, the central bank cut the discount rate from 12 percent to 10.5 percent in June, and further to 9 percent in October. Treasury bill rates declined during the year by about 5 percentage points to 9 percent at end-December.

12. **All quantitative performance criteria and benchmarks for end-March, June and September 2001 were met, with the exception of those on revenue for each of the quarters.** At end-December 2001, the performance criterion on the central bank's net foreign assets, adjusted for a shortfall in foreign currency privatization receipts and in donor disbursements, was met by a significant margin; however, the performance criterion on net domestic assets of the central bank was not met because advances to the state petroleum company, SOLIMA, under liquidation, were not reimbursed by the government before year's end, as envisaged. The end-December 2001 performance criterion on domestic government financing was not met because the large shortfall in external financing (SDR 49.5 million) exceeded the SDR 30 million cap in the adjuster (Appendix I, Table 1); the performance criterion on the floor on tax revenue was also not met. The authorities are requesting waivers for the nonobservance of these performance criteria, in view of the recent corrective actions undertaken to strengthen revenue performance, and the actions taken to close the operations of SOLIMA and to undertake its audit (MEFP, para. 29).

13. **In 2001, the authorities implemented satisfactorily the envisaged structural reforms in the areas of budgetary management, tax administration, and privatization** (see Appendix I, Table 2). The computerized customs information system (ASYCUDA 2.7) was installed in the secondary ports, but the upgrade to the 3++ version was delayed, so that the related structural benchmarks for end-September and end-December 2001 were missed. A United Nations Conference on Trade and Development (UNCTAD) technical assistance mission to secure its installation is expected shortly.

14. In the period 1997-2001, the incidence of income poverty declined in the urban areas from 63 percent to 50 percent, but remained broadly stable in the rural areas, at about 75 percent (see Table 14 and the analysis contained in the interim PRSP, EBD/00/105, 12/4/00). United Nations Development Program (UNDP) estimates indicate that in the first half of 2002 the national poverty rate rose by 6 percentage points, from 69 percent in 2001 to 75 percent. Poverty and extreme poverty have remained very high in rural areas since 1993, showing almost no improvement. This reflects stagnant agricultural productivity and points to the need for significant rural development, including better extension services and access to markets through improved rural roads. A set of social indicators is presented in Table 14.

15. **In recent years, Madagascar has liberalized and simplified its external trade regime.** Since October 2000, the country has been a member of the free trade area under the Common Market for Eastern and Southern Africa (COMESA), and since early 2000 it has had a preferential tariff agreement with Comoros and Mauritius;[2] both agreements provide for a 100 percent tariff reduction. It adopted in 2000 a five-rate external tariff structure with a

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[2] At present, nine countries are members of the COMESA free trade area: Djibouti, Egypt, Kenya, Madagascar, Malawi, Mauritius, Sudan, Zambia, and Zimbabwe. Madagascar's trade with Mauritius is significant, with exports and imports from Mauritius accounting for 4 percent and 10 percent of the respective totals. Trade with COMESA countries other than Mauritius is negligible.

maximum tariff of 30 percent, consistent with the commitment under the Regional Integration Facilitation Forum (RIFF), and the numbers of products subject to the 30 percent rate was reduced both in 2000 and 2001, in line with RIFF commitments. With a November 7 presidential decree, rates on intermediate inputs for agriculture and textiles, and on some construction materials, were brought to zero, and the rates on some machinery and intermediate goods were reduced to a maximum of 25 percent (see MEFP, paras. 14 and 15). Madagascar has an open trade regime; according to the Fund's overall trade restrictiveness index, it is rated 3 on the 10-point scale of restrictiveness (10 indicating the most restrictive). In 2001, Madagascar's average tariff rate (including the statistical tax on imports and stamp duties) was 17.2 percent, and very few nontariff barriers are maintained.

III. The 2002 Political Crisis and Its Economic Impact

16. **The presidential elections of December 16, 2001 led to a major political crisis,** as Mr. Ravalomanana, the leading challenger and then mayor of Antananarivo, claimed a first-round victory, which was then contested by the incumbent President, Mr. Ratsiraka. The High Constitutional Court (HCC) ruled in late January that no candidate had received the absolute majority needed to avoid a runoff. This triggered massive demonstrations by Mr. Ravalomanana's supporters, followed by a general strike in the capital, while Ratsiraka's camp organized an economic embargo of the central plateau, blockading all roads and bridges.

17. In late February, Mr. Ravalomanana proclaimed himself President and formed a new government, while Mr. Ratsiraka's government withdrew to the coastal city of Toamasina (Tamatave). The latter assumed control of a number of branches of the central bank, while the headquarter's management expressed allegiance to Mr. Ravalomanana; this duality led foreign depositories to freeze Madagascar's external reserves, bringing about the suspension of trading in the interbank foreign exchange market. Following a recount of votes in early May, the HCC reversed its decision and declared Mr. Ravalomanana the winner of the election. He was officially inaugurated on May 6, and, with the military shifting to support him, he was able to take control of almost the whole country by end-June, prompting the departure of his opponent from Toamasina on July 5.[3]

18. **The crisis brought economic activity in the secondary and tertiary sectors to a virtual standstill: tourism ground to a complete halt, while agricultural activities and production were less affected**. The February general strike and subsequent blockade of the central plateau severely disrupted energy supply and production. According to surveys of the export processing zone, industrial production declined by about 80 percent in the first six months of 2002, compared with the same period in 2001; an estimated 80,000 workers were temporarily laid off. The Malagasy authorities estimate that the pronounced decline of economic activity during the crisis will result in a 12 percent drop in real GDP in 2002. With

[3] By early-July, all major countries had recognized the Ravalomanana government.

the loss of jobs and the increase in the price of essential goods, poverty increased markedly, while utilization of social services declined sharply, as discussed below.

19. Consumer prices rose by 21 percent in the first five months of 2002, as a result of shortages of oil, electricity, and a number of essential goods. In June and July, when supplies of fuel and other necessities became available throughout the country, consumer prices started to fall; from end-May to end-October, the CPI declined by 6.1 percent. The year-on-year rate of inflation is projected at 12 percent by end-December 2002.

20. **Commercial banks continued to operate throughout the crisis**, but foreign exchange transactions were limited, as the interbank foreign exchange market was closed. In addition, treasury bill auctions were suspended throughout the crisis, and all outstanding bills were rolled over. At the reopening of the foreign exchange interbank market in early August, the Malagasy franc depreciated by 12 percent vis-à-vis the euro, and by 11 percent in nominal effective terms; it has remained relatively stable in the following months, as the large inventories built up at the harbors during the crisis reduced the need for new imports, other than fuel. As a result of the clearance of external arrears on debt service incurred over the first half of the year, and of central bank sales of foreign exchange to fuel importers, international reserves fell by SDR 60 million between June and September; they rose in October, as the World Bank disbursed a US$42 million tranche under SAC II. At the reopening of the treasury bill market in October, interest rates rose by about 3 percentage points.

21. **Budgetary revenue fell sharply during the crisis, owing to the contraction of economic activity, employment, and imports.** In the first six months of the year, tax revenue totaled FMG 857 billion, a decrease of 44 percent from the same period in 2001. In the July–October period, both customs revenue and domestic tax collection increased, owing also to collection of back taxes and the intensified fight against fraud at customs. In the first six months of the year, base wages and pensions were paid regularly, and significant resources were allocated for military operations, whereas other operating expenditures were kept to a minimum. During the crisis and in the remainder of the year, the government decided not to pay a number of personnel allowances and indemnities because of the revenue shortfall. The sharp downturn of revenue in early 2002 prevented the treasury from settling, as customary, the payments orders that were issued toward the end of 2001;[4] these arrears were not fully paid until October and November 2002. Moreover, arrears for value-added tax (VAT) credits owed to enterprises continued to rise over the first part of the year, so that by end-September VAT-related arrears to EPZ enterprises and other companies had amounted to FMG 97.5 billion and FMG 67.5 billion, respectively, or 0.5 percent of GDP in total. The arrears to EPZ companies were cleared in October and November, and those to other companies are to be fully repaid by end-2002.

[4] Outstanding payments orders at the treasury at end-2001 amounted to FMG 424 billion, equivalent to 1.4 percent of GDP.

22. **The crisis had a negative impact on the most vulnerable groups**, with an estimated 6 percent increase in income poverty in the first half of 2002 (from 69 percent to 75 percent). It led to a sharp decline in health centers' utilization because of their cost, as well as a reduction in school enrollment.[5] Farmers' net income was affected by the increase in the transportation costs and decline in farm gate prices, because of marketing difficulties. To assist the population, the government decided in early October to eliminate primary school attendance and user fees for primary health centers for a six-month period. The cost of these measures, estimated at FMG 60 million (0.2 percent of GDP), will be covered by the HIPC Initiative relief budget. Community-based projects in the areas of nutrition and integrated rural development are playing an important role in combating the temporary increase in poverty.

23. Indicative benchmarks for end-March 2002 on net foreign assets and net domestic assets of the central bank, and on domestic financing of the government were met, whereas that on fiscal revenue was not. Because of the freezing of external reserves, arrears with some multilateral and bilateral creditors were accumulated, all of which were promptly settled as soon as access to the external reserves was restored in July.[6] Accordingly, the authorities are requesting a waiver in respect of the breach of the corresponding performance criterion.

IV. Policy Challenges and the Pprogram for 2002-2003

A. Policy Challenges

24. The new authorities acknowledged that the country has experienced a relatively high growth rate in recent years, but underscored that this had not contributed to a significant reduction of poverty, nor was accompanied by a substantial improvement in social indicators. Their aim is to address these serious shortcomings, and stimulate growth by a faster execution of a comprehensive investment program geared at improving physical and social infrastructure. They also consider that the previous government was influenced by entrenched interests, and had not fought corruption adequately, with negative effects on resource mobilization. While they considered that past Fund policy advice had been broadly appropriate, in particular with its focus to strengthening public finance management and tax administration, they thought that progress in these areas had been inadequate and had to be accelerated. They were particularly committed to increase transparency and accountability at all levels of government.

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[5] The health centers' utilization rate declined by 36 percent in rural areas and 14 percent in urban areas, and school dropout rates rose to 14 percent, up from 9 percent, according to World Bank and UNDP estimates.

[6] Obligations to the Fund and the World Bank falling due in the first half of 2002 were paid on time, as the two managements of the central bank cooperated in accessing a reserve account at the Bank for International Settlements (BIS).

25. Because of their preoccupation with fostering the economic recovery and resolving pressing financial issues that were threatening the viability of private sector enterprises, and the need to prepare a credible 2003 budget, the authorities were not ready to discuss in depth a medium term scenario beyond 2003. This will be developed in the coming months in the context of the finalization of the PRSP, which will contain a medium-term macroeconomic framework, including expenditure in the priority sectors consistent with the overall medium-term budgetary outlook. In this regard the staff urged that the revised medium-term framework be based on a thorough analysis of the sources of growth, and aimed at promoting investment and savings in an environment of improved governance. The authorities concurred with the staff that the medium-term budgetary scenario needed to include a realistic increase in the domestic revenue effort with cautious projections regarding external assistance, mostly project related, and a very modest recourse to domestic financing, in view of its cost.

26. Following a drop in real GDP of about 12 percent in 2002, a recovery of 8 percent is expected in 2003; in the discussions, the staff stressed that growth of 5–6 percent a year could be achieved over the medium term and even exceeded, provided savings and investments would pick up, with a balance between private sector investment directed to exports and public investment aimed at improving infrastructures and social services, in particular in the rural areas. There are good prospects over the medium term in the EPZ, tourism, construction and mining, and possible higher agricultural production, but the staff underscored that realizing this potential required strong improvements in the quality and efficiency of public administration, as pointed out in the recent Integrated Framework report.[7] The authorities concurred with this view, and noted that the need for improved governance would be a central theme in the revised PRSP.

27. Inflation is expected to decline from 12 percent at end-2002 to 5 percent next year, and average 3–4 percent over the medium term. After falling significantly in 2002, both export and import volumes are expected to recover substantially in 2003, and then to grow at about 6–7 percent per annum. The current account balance, including transfers, is projected to widen from 1.3 percent of GDP in 2001 to 4.5 and 5.7 percent of GDP in 2002 and 2003, respectively, before stabilizing at about 5 percent of GDP until 2006. Underlying this external current account trend is the view that investments and savings can increase by about to 2 to 3 percentage points of GDP, from the level projected for 2003 (Table 13).

28. The economy is subject to important vulnerabilities that highlight the need for diversification: the agricultural economy is highly exposed to climatic adversities, such as drought and cyclones, and sharp fluctuations of commodity prices; the political system has experienced recurring bouts of instability, which could deter potential investors; and the

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[7] A 2001 report on Madagascar prepared in the context of a pilot study of the integrated framework, under the auspices of the World Trade Organization (WTO), highlighted that inefficiencies and petty corruption at the level of customs administration, the ports, and the roads were major impediments to the expansion of industrial production and exports.

textile and apparel sector is exposed to intensive foreign competition, and its prospects could be adversely affected by the expiration in 2005 of the Multifiber Agreement. Thus, there is a need to widen the specialization of the EPZ, now very concentrated in apparel, expand agricultural activity to new products, while increasing the sector's productivity, and make better use of the favorable opportunities in tourism and mining.

29. In discussing the fiscal framework, the staff underscored that the large need to improve infrastructure and basic social services calls for significant progress in domestic revenue mobilization, as, judging from the recent donors meeting, external financial assistance is likely to stabilize over the medium term as a ratio to GDP, after an expected increase in 2003. The budgetary revenue as a ratio to GDP in Madagascar was lower than in other comparable countries of the region, and there was a potential for substantial revenue increases through improved tax administration. The authorities concurred, but noted that improvements in this area would require extensive technical assistance, which they had already requested from the Fund and other donors.

B. The Poverty Reduction Strategy

30. **The poverty reduction strategy will be fully elaborated in the PRSP, which is now expected to be completed in March 2003, after its submission to the new national assembly**. Following intensive discussions with civil society and donors in 2001, additional regional seminars were held in the second half of 2002, focusing on poverty and the environment. The document will give prominent emphasis to the need to improve governance at all levels of government, including the judiciary and regulatory agencies. The fight against poverty, which is still pervasive in Madagascar, will rely on strengthening community-based development projects, improving the provision of social services, and promoting income growth in the rural areas. The PRSP will include a costing of the priority action programs, which will have to be consistent with the budgetary framework, and detailed monitoring mechanisms.

31. Consistent with the interim PRSP and progress reports, financial policies in the remainder of 2002 and 2003 will focus on maintaining macroeconomic stability, while mobilizing additional revenue from domestic sources to complement external assistance for budgetary support and project financing. Structural reforms will seek to improve the quality and transparency of public administration, and strengthen the judicial, regulatory, and control systems, while continuing the restructuring and privatization of public enterprises. To promote agricultural development, which is essential to fight poverty, emphasis will be placed on the maintenance and improvement of rural roads, largely neglected in the past, deepening the microfinance network, and strengthening extension services.

C. Fiscal Policy

32. **The discussions on fiscal policy for the remainder of 2002 and for 2003 centered on the need to reduce arrears, the revenue effort to be pursued, and the improvement in expenditure management**. The authorities agreed with the staff that a key priority was to

reduce the stock of domestic arrears that were hurting the private sector, including export-oriented firms, which had accumulated a large amount of VAT credits. This required containing domestic expenditure for infrastructure, also viewed as a key priority by the government; meanwhile, efforts should be made to accelerate the execution of projects funded with foreign concessional assistance. The authorities agreed that there was a pressing need to streamline procedures for VAT payments by the EPZ firms, to avoid a future accumulation of VAT credits, which threatened the financial viability of exporting firms and deterred potential new investors. The government recognized that domestic revenue mobilization was a key challenge for the period ahead and the medium term, and stressed that combating fraud at customs was a critical priority. To that end, a number of actions are under way, including extensive personnel changes. The government is keen to reduce customs duties on a number of essential imports to foster growth—an objective that calls for higher receipts from domestic taxation.

33. **The overall budget deficit, excluding grants, is projected to decline from 8.1 percent of GDP in 2001 to 7.7 percent of GDP,** as the fall in the revenue-to-GDP ratio, from 10 percent to 7.3 percent, will be more than offset by the drop in both current and capital expenditure as a share of GDP. The increase in external budgetary assistance in the last quarter of 2002 (MEFP, para. 20) will permit a reduction in domestic arrears 0.6 percent of GDP over the year, including the repayment of all VAT of EPZ and other companies. In 2003, the deficit, excluding grants, is projected to decline further to 7.4 percent of GDP. The authorities agreed with the staff that only temporary bank financing of the deficit should be envisaged in 2003, as the central bank advances to the government already exceeded the statutory limits and commercial banks were not likely to permanently increase their holdings of treasury bills, although some seasonal increase could be envisaged. A remaining financing gap of about 0.1 percent of GDP is expected to be filled by additional budgetary aid, from the African Development Bank (AfDB) and bilateral donors.

34. **The revenue-to-GDP ratio is targeted to rebound to 10.5 percent of GDP in 2003, up from 10 percent in 2001.** A major effort is under way to strengthen the tax and custom administrations, with improved computerization at customs, cross-checks, and an enhanced campaign against fraud and sales without invoices (MEFP, paras. 21, 22, and 34). The implementation of the unified tax on small businesses, delayed by one year because of the need to simplify collection modalities, will widen the revenue base. The reduction of customs duties introduced in November 2002 is estimated to cost 0.1 percent of GDP on an annual basis; to offset partially this reduction, excise taxes on cigarettes and motor oil have been increased.

35. **In 2002, total expenditure, as a share of GDP, is projected to be lower by 2.3 percent of GDP, compared with 2001,** as expenditure on personnel and goods and services has been rigorously limited in the second half of the year, in view of the shortfall in revenue. Capital expenditures will also be one-third less than in 2001, after the suspension of a number of projects in the first part of the year; on-lending to public enterprises in the context of their restructuring and privatization (see below, and MEFP, para. 31) will amount to 0.7 percent of GDP. Priority expenditures in the areas of education, health, rural roads, water,

and sanitation, financed by the HIPC Initiative debt relief, will amount to 1 percent of GDP in both 2002 and 2003. Extensive consultations with the donor community have taken place to better target these expenditures and actions are underway to improve their tracking; quarterly execution reports will be prepared in 2003 (see Box 2).

36. **In 2003, total expenditure will reach 17.8 percent of GDP, up from 17.3 percent in 2001.** The increase in base salaries will be limited to 12 percent, matching the year-on-year rate of inflation at end-2002. The ratio of the wage bill to GDP will increase by 0.8 percentage points of GDP, reflecting the resumption of the payment of allowances to senior civil servants and of emoluments to parliamentarians, suspended in 2002, the payment of bonuses to teachers in rural areas—a priority need financed by HIPC resources—and higher indemnities to security personnel. With the resumption of real GDP growth, this ratio is expected to decline after 2003. Capital expenditures are projected to reach the equivalent of 7.2 percent of GDP, the same level as in 2001, following a sharp drop in 2002; within this total, foreign financed capital spending will increase by 42 percent from the 2001 level, as donors are committed to increasing the pace of disbursements on existing projects. The execution of foreign-financed projects will benefit from faster procedures for the payment of government contributions to the projects, including the VAT (MEFP, para 16).

37. **A comprehensive effort will be made to improve treasury accounting, accelerate the execution of expenditure, and strengthen the monitoring of budget implementation (MEFP, paras. 23 and 24), which are also key HIPC Initiative completion point triggers (see Box 3)**. To these ends, (i) the compilation of monthly treasury balances is being accelerated; (ii) the prior approval by the expenditure control directorate of commitment expenditure will be accelerated; and (iii) the provincial budgetary directorate will be strengthened, with World Bank assistance, in order to centralize expenditure data and enable the preparation of quarterly budgetary execution reports. A concerted effort is also being made to reduce delays in preparing budget execution laws. It is expected that six ministries will compile quarterly budgetary execution reports by end-2003, up from two ministries (health and education) at present, and that reports covering all ministries will be prepared in 2004.

D. Monetary Policy and the Financial Sector

38. **There was a consensus that monetary policy will have to be geared to containing inflationary pressures, while being supportive of the private sector's credit needs.** To that end, no expansion of net credit to government is envisaged in 2003, other than for onlending of Fund credit, as noted above. As the increase in the net foreign assets of the central bank would contribute 4.7 percentage points to monetary growth, a 15.4 percent increase in credit to the private sector in 2003 would be consistent with an aggregate expansion of 12.5 percent of broad money, in line with the expected growth of nominal GDP (Tables 6, 7, and 8).

39. Following the privatization of the two remaining state banks in 1998-99, the authorities adopted a number of measures in 2000-01 to enhance the soundness of the banking and financial system, including limitations on insider lending, lower

Box 2. Madagascar: Status of Actions to Strengthen Tracking of Poverty-Reducing Public Spending

	Actions	Timing (S/M)[1]	Status (FI/II/ NS)[2]	Date Achieved	Comments
Actions to strengthen budget formulation					
1	Identify poverty-reducing items in budget	S	FI	07/01	
2	Introduce medium-term expenditure framework (MTEF)	M	NS		MTEF to be considered after IFMIS is operational (item 5).
Actions to strengthen budget execution					
3	Prepare quarterly budget execution reports for the Ministries of Health and Education	S	FI	09/01	
4	Implement integrated financial management information system (IFMIS) pilot project in Tamatave	S	FI	09/02	Extension to other provinces being studied.
5	Introduce fully functional IFMIS	M	NS		Dependent on item 4.
Actions to strengthen budget reporting					
6	Computerize treasury operations in 22 principal treasury offices	S	FI	11/01	
7	Prepare monthly closing accounting balances for the treasury	S	II		Balances for 2000 to be completed by end-2002. Balances for 2001 and 2002 will be prepared in 2003. Starting in early 2004, monthly balances will be prepared on a timely basis.
8	Prepare budgetary execution laws (*loi de réglement*) 1999-2001	S	II		The 1999 report is expected before end-2002.The 2000 and 2001 reports are expected before end-2003.
9	Initiate quarterly budget execution reports for Ministries of Public Works, Rural Development, Water and Forests, and Justice	S	II		
10	Initiate quarterly HIPC budget execution report	S	II		First report expected at end-March 2003.

[1]S=Short-term action; M = medium-term action.

[2]FI=fully implemented; II= implementation initiated; NS=not started.

Box 3. Progress Toward HIPC Initiative Completion Point Triggers

The triggers for the floating completion point under the enhanced HIPC Initiative are reported in Box 8 of the HIPC Initiative decision point document (12/5/00). The specific triggers (in addition to the implementation of a full PRSP for at least one year, the use of budgetary savings from interim debt-service relief in accordance with the criteria set at the decision point, and the maintenance of macroeconomic stability through satisfactory implementation of the PRGF-supported program) include the following: **(A) actions in the area of financial monitoring and control; (B) the establishment of a public and transparent information system for the granting of licenses in mining, fishing, and forestry sector; and (C) the improved delivery of basic services.**

Triggers	Status
A1. Financial monitoring and control have been improved as follows:	
(a) Control systems have been strengthened through (i) adoption of an appropriate legal and constitutional framework; (ii) adoption of procedures and internal control systems that conform to international technical standards; and (iii) an increase in staffing and resources of the State Inspectorate General (IGE) and the Commitment Control Office (CDE).	A comprehensive study was completed by an independent consultant in April 2001, covering also the Auditor Court (Chambre des Comptes) and the Procurement Commission (Commission des Marchés); the report's recommendations were adopted by the government in June. The related plan of action centers on reforming the statutes governing these agencies, including assigning external auditing functions to the Procurement Commission and internal auditing functions to the State Inspectorate General, preparing detailed manual of procedures, increasing reporting obligations of public institutions, and strengthening the equipment and staffing of control agencies. Initial actions have included the recruitment of additional staff for the agencies during 2001. Additional resources have been assigned to the agencies in the 2002 budget.
(b) A monitoring system for the budgetary cycle (*engagement, liquidation, mandatement, paiement*) has been designed and implemented in at least six ministries, including the Ministries of Basic Education and Health.	The system is presently operational for the Ministries of Health and Basic Education. It will be expanded in 2003 to cover also the Ministries of Public Works, Rural Development, Forestry and Water, and Justice
(c) Starting in 2001, the centralization procedures and consolidation of all balances of the principal treasury offices by the Central Treasury Accounting Office (ACCT) have been improved through the formation of a consolidation unit, constituting a step toward the establishment of general balance sheet statements and of reliable opening and closing accounting balances.	In 2001, all the 22 principal treasury offices were computerized; initial and closing balances have been established for the period 1993-98. The balances for 1999 and 2000 will be established before end-2002, and by early 2004 the accounting system will be current.
(d) The 1999 budgetary execution law (*loi de règlement*) was prepared during 2001 and the 2000 budgetary execution law was prepared before end-June 2002.	The 1999 law was sent to the Auditor Court (Cour des Comptes) in late 2002; those for 2000 and 2001 will be submitted during 2003.

Box 3. Progress Toward HIPC Initiative Completion Point Triggers (concluded)	
A2. Biannual reports on education and health sector activities at the central and decentralized level have been prepared, including (i) budgetary allocation and expenditure execution; and (ii) physical achievements.	Quarterly budgetary allocation reports are being regularly compiled. No physical outcome reports have yet been prepared.
B. A public and transparent information system on granting licenses (beneficiary list, geographical zone, and amount) in the mining, forestry, and fishing sectors has been implemented. The list will be published biannually.	For the mining and fishery sectors, the information on licenses exists but is not accessible to the public.
C1. Teacher availability in rural areas has been expanded by (i) formalizing and implementing new financial incentives for teachers to serve in rural public primary schools; and (ii) recruiting at least 3,500 new teachers from 2000 onward for public primary schools and deploying at least 60 percent of them to schools with contractual teachers or with a ratio of pupils to publicly paid teachers in excess of 50.	In 2001, 4000 teachers were recruited and assigned to the rural areas; the system of financial incentive has been established.
C2. The generic essential drug supply system of district pharmacies has been rendered operational (including the start-up of generic drug availability for hospital outpatients), as measured by an increase in the annual gross revenues of the existing central purchasing pharmacy.	At present, the central agency is operational; however, its functioning was not satisfactory in 2001, with delays in launching the tenders for the generic drugs. Improvements have been made in the second half of 2002, when the agency has been recapitalized.
C3. Current road maintenance needs are covered 100 percent through the Road Maintenance Fund, of which at least 10 percent are used for rural roads.	The functioning of the Road Maintenance Fund was unsatisfactory in 2001, with government transfers irregular. The financing of the fund was strengthened in August 2002 with the increase of the special levy for its budget in the price structure of petroleum prices.

ceilings on risk concentration, and tighter requirements on internal audit systems. They have also tightened the licensing requirements for microfinance institutions. The authorities have requested Fund technical assistance to strengthening bank supervision, including the establishment of an early warning system (MEFP, para. 28). The authorities are of the view that the increase in the nonperforming loans will reverse in the coming year, as the economy strengthens. Box 4 presents banking sector soundness indicators.

40. The authorities are committed to promoting financial intermediation, in particular by removing various impediments to bank lending. A major barrier to increasing private sector credit is constituted by restrictions on foreign holdings of real estate; banks, being foreign owned, are hampered in their ability to execute real estate guarantees, thus curtailing access to credit by small and medium-size enterprises.

E. Other Structural Reforms and Governance Issues

41. **The government is determined to improve the investment climate and the regulatory environment for private sector activity,** and has taken a series of measures to encourage the return of foreign investors, who, during the crisis discontinued their operations in the EPZ. These measures include the speeding up of VAT refunds; the adoption of a decree in early November allowing EPZ companies to defer payment of VAT on inputs; and actions to streamline controls at customs for companies with a strong compliance record. A reform of the regulations pertaining to VAT on investments is also under preparation (see MEFP, para. 16). The government is committed to accelerating reforms of commercial law and to improving the functioning of the judicial system, with the assistance of a number of donors.

42. **With regard to public enterprises, a number of actions are under way to accelerate the restructuring and privatization of key companies (MEFP, para. 31).** The government expects to conclude before end-2002 the negotiations for the sale of the telephone company, TELMA. It has placed the airline company, Air Madagascar, under a management contract with Lufthansa Consulting, and the new management is implementing a number of measures to secure a positive cash flow in 2003, thereby placing the company in a stronger position for a future possible privatization. A meeting with foreign creditors to obtain debt reduction will take place before end-2002. In early October, the northern railroad network was given in concession to a new company, MADARAIL, with foreign majority participation, with the aim of achieving a rapid rehabilitation of the network. To improve management of the electricity and water company, JIRAMA, the government plans to place the company under a management contract with a specialized foreign firm; measures are also under preparation to strengthen collection of electricity and water bills from local authorities, and a study to recommend tariff adjustments is to be completed shortly.[8] The cotton ginning

[8] On December 2, 2002, the government paid a part of the arrears of local authorities to JIRAMA, which, in turn, paid overdue bills to fuel suppliers (see MEFP, para. 32); this constituted a prior action for completing the second review under the PRGF (MEFP, para. 41 and Appendix I, Table 4)

Box 4. Madagascar: Soundness of the Banking Sector

The financial indicators reported in the table below indicate that the Madagascar banking sector has exhibited a steady improvement over the past three years, particularly after the restructuring of two state-owned banks in 1997-98. Notwithstanding a deterioration in results over the first half of 2002 due to the crisis and an increase in nonperforming loans, the banking sector remains sound; however, the recent increase in nonperforming loans suggest that this aspect will have to be monitored carefully. The capital adequacy ratio of the banks is well above the minimum requirement of 8 percent. The profitability of banks has been very high in 2000 and 2001, with a return on equity reaching 51 percent in 2001. It is also to be noted that the banks have maintained since 1999 a very high liquid assets position.

Madagascar: Banking Sector Soundness Indicators, 1997-2002
(Ratios in percent)

	1997	1998	1999	2000	2001	2002 Sep.
Capital adequacy						
Regulatory capital to risk-weighted assets[1]						
Bank with lowest ratio[2]	...	...	10.0	...	12.0	12.5
Assets quality						
Nonperforming loans to total gross loans	38.2	21.1	8.4	8.4	10.3	17.7
Earnings and profitability						
Return on assets	...	3.6	4.9	5.0	4.0	...
Return on equity[3]	...	43.7	50.3	62.9	50.8	...
Noninterest expenses to gross income	49.2	46.5	42.8	45.4	48.9	51.2
Liquidity						
Liquid assets to total assets (liquid assets ratio)	45.8	39.4	41.5	40.1	38.9	43.8
Liquid assets to short-term (demand) liabilities[4]	75.9	63.2	66.1	69.0	60.3	70.3

Source: Commission de Supervision Bancaire et Financière.

[1]Regulatory capital = tier I + tier II capital.
[2]The 2002 ratio refers to end-August 2002.
[3]Shareholders' equity includes paid-up capital, share premiums, capital grants, and retained earnings.
[4]Demand liabilities include savings deposits.

and marketing company, HASYMA, will be restructured with the opening of its capital to additional foreign shareholders in the coming months. In the sugar sector, the government is finalizing the strategy for opening the capital of the state sugar company, SIRAMA, to foreign participation. The strengthening of the cotton and sugar sectors is expected to contribute to farmers' income growth and to alleviate poverty in rural areas.

43. **The government is determined to fight corruption at all levels (MEFP, para. 21).** To that end, in September an anticorruption commission was appointed and given the task of preparing a national plan for good governance, possibly including the establishment of an anticorruption authority. The government has carried out an audit of the 2001 transactions of the special budgetary funds at the disposal of the presidency and the prime minister's office, and has adopted a decree under which the special funds are subject to semiannual audits by the Audit Court; it has also instituted an obligation for all members of the government and senior civil servants to disclose their assets on an annual basis.

F. External Sector Issues

44. **Following the sharp deterioration in the balance of payments in the first nine months of 2002, the overall balance is expected to improve significantly in the last quarter, reflecting large disbursements by the World Bank, European Union, and other donors.** Thus, the net reserve loss for the year is expected to be contained at SDR 30 million, following a reserve loss of SDR 73 million in the first nine months (Table 9). In 2002, the current account deficit, including grants, is expected to widen to 4.5 percent of GDP, up from 1.3 percent in 2001, as exports are projected to drop by 46 percent in SDR terms during the year. EPZ exports are expected to fall by some 70 percent, as new orders are reviving slowly and only 49 of 142 EPZ enterprises had even partially resumed operations by end-September. Vanilla export receipts are also expected to fall in 2002, as a result of lower quality and a decline in international prices in the second half of 2002.[9] Imports will also contract significantly during the year, with only a gradual recovery in the last part of 2002, as household consumption and business inventory rebuilding remain weak. Foreign direct investment in 2002 has fallen sharply.

45. **In 2003, the current account deficit, including grants, is projected to widen further to 5.7 percent of GDP.** The expected rebound in total exports (32 percent in SDR terms), spurred by EPZ exports, is likely to be offset by an increase in imports of the same magnitude, as public and private investment and domestic consumption recover. Higher external assistance and direct investment are projected to lead to a reserve accumulation of about SDR 23 million. Total gross external assistance, including debt relief, could reach SDR 344 million, or 9.3 percent of GDP, with an increase in the project finance component

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[9] Because of increased security concerns in 2002 and mounting theft, farmers opted to harvest earlier than optimal, with a negative impact on the quality of the crop.

to 4.6 percent of GDP, up half a percentage point of GDP from 2001. A remaining financing gap of SDR 34 million is expected to be covered by additional multilateral and bilateral assistance, including from the AfDB.

46. **The discussion with authorities on the medium-term balance of payments outlook focused on the need to attract foreign investment and diversify exports, as well as on the assessment of risks for key export activities.** The baseline scenario for the balance of payments assumes an average annual increase in exports of 9.4 percent in SDR terms between 2003 and 2006, largely led by a strong performance of EPZ firms; average annual import growth would be 8.6 percent in SDR terms during the same period. The outlook is highly dependent on a solid pickup of activity in the EPZ and the continued attractiveness of the country as a destination of foreign investment, which, in turn, requires continued moderation in labor costs and a rapid improvement in customs and port administration, as discussed below.

47. **External borrowing in 2001–02, and the profile of future borrowing, remain very close to that presented in the HIPC Initiative decision point document** (see Table 10 and Figure 4). The delivery of HIPC Initiative assistance by creditors is presented in Table 11. External financial assistance during 2004–06, excluding debt relief, is expected to remain above 6 percent of GDP, with grants accounting for about half of the total. This should contribute to a steady accumulation of gross reserves to about 16 weeks of imports in 2004–06, up from 14 weeks in 2001. Indicators of financial obligations to the Fund are reported in Table 12.

48. **The authorities acknowledged during the discussions that an exchange rate appreciation could jeopardize export competitiveness.** The 11 percent depreciation in the nominal effective exchange rate so far in 2002 has partly reversed the appreciation during 2000 and 2001. While the real effective exchange rate, measured on the basis of relative CPI, has appreciated further in 2002, wages have been stable during the year, so that in terms of unit labor costs the real effective exchange rate has depreciated. Industrial exporters indicated that, given the relatively low wage level and the good skills of the labor force, production facilities in Madagascar were highly competitive; this was corroborated by the continued interest of new investors in locating in the country. The exporters noted, however, that the quality of the operating environment (speed of port clearance, roads, and administrative and customs clearance procedures) was essential to investment decisions, and they had made clear to the authorities that they expected rapid improvements in all these areas.

49. **Bilateral agreements with Paris Club creditors**, under the March 2001 Agreed Minute providing for Cologne terms (90 percent reduction in net present value (NPV) terms), are expected to be finalized by end-2002.

50. It is expected that the completion point under the HIPC Initiative will be reached by March 2004, after one year of implementation of the PRSP.

V. Program Monitoring

51. As indicated in the MEFP, implementation of the program will be monitored with quantitative and structural performance criteria and benchmarks (Appendix 1, MEFP, Tables 3 and 4). The structural measures focus on the areas of tax policy and administration, expenditure management and auditing, and financial sector reforms, including reforms at the central bank in compliance with the Fund's safeguards assessment policy. They are essential to correct key weaknesses in budgetary management, and to strengthen the central bank. These measures are complemented by structural measures monitored by the World Bank. In addition, the European Union and bilateral donors provide support in the areas of legal and judicial reform, capacity building, and financial sector development. The next semiannual review under the current arrangement is expected to be completed in May 2003.

VI. Technical Assistance, Data Issues, and Safeguards Assessment

52. Madagascar has been receiving extensive technical assistance from multilateral and bilateral donors over the past several years. Most recently, the Fund's technical assistance has focused on securing improvements in public expenditure management and treasury accounting, and in balance of payments and monetary statistics. The authorities have recently requested Fund assistance in the areas of tax and customs administrations and policy, treasury management, international reserve management, banking supervision, and the central bank internal audit; assistance in all these areas will be provided in the coming months.

53. The mission discussed with authorities the progress on the implementation of recommendations of the balance of payment statistics mission to Madagascar in June 2001. The authorities noted that the reactivation of the committee in charge of finalizing external trade statistics had already contributed to improvements in data collection and analysis. Significant progress was also made on the implementation of banking sector surveys, aimed at ensuring comprehensive coverage of service transactions in the balance of payments. The first phase of the installation of the new system of banking sector surveys on resident/nonresident transactions was launched in August 2002, with full implementation of the new system expected by end 2002.

54. Under the current PRGF arrangement, the Central Bank of Madagascar is subject to a full Stage One safeguards assessment policy. The safeguards assessment completed on November 12, 2001 recommended that the central bank move toward adopting International Accounting Standards (IAS), strengthen its audit function, and perform an internal audit of its reserve management- and foreign exchange-related activities. Consistent with these recommendations, the central bank is committed to disclosing in its annual report for 2001, which will be finalized shortly, the key differences between IAS and the present accounting

framework, which can be changed only by law;[10] an activity plan for the audit department will be established by end-March 2003, and the reporting system of the department will be strengthened. An audit of the external reserves will be completed by end-June 2003.

VII. Staff Appraisal

55. **Madagascar's performance under the PRGF-supported program in 2001 was strong, with the exception of weak revenue collection, an issue that the new government has begun to address.** Economic activity was buoyant, spurred by a rapid expansion in production and exports of the EPZ, and by a substantial increase in foreign direct investment. Inflation abated, and international reserves increased substantially more than programmed. These results were reversed, however, by the political crisis of the first half of 2002, which caused widespread shortages, a sharp fall in industrial activity, an increase in inflation, a fall in real incomes, and a significant increase in poverty. Despite the favorable growth performance over the 1997-2001 period, rural poverty did not decline, highlighting that development in agriculture has been inadequate.

56. The new government that took office in mid-2002 is determined to achieve faster growth, a rapid improvement in social indicators, and a decline in poverty, in particular in the rural areas. To these ends, it intends to rely on a rapid implementation of an ambitious public investment program, mostly foreign financed, better prioritization of expenditures, and a more favorable climate for private sector investment. It has also taken measures to alleviate the increased poverty and reduced utilization of social services caused by the crisis. It has set as a paramount objective the fight against corruption and improvement of transparency and efficiency at all levels of public administration, aware that the needed investment will not materialize if the administrative environment does not improve significantly. The staff commends the authorities for the measures already taken in this area, including the establishment of an anticorruption commission, the strengthening of the role of the Audit Court, and changes of personnel at customs. Given the magnitude of the task, a comprehensive and sustained effort in a large number of sectors will be needed, including reforms in the remuneration system of civil servants, which will have to be better linked to performance.

57. **The staff is encouraged by actions already taken at the customs administration to combat fraud, but these efforts will have to be sustained with determination, given the extensive weaknesses.** At the same time, there is a need for streamlining administrative procedures, in order to ensure that delays at customs and ports are not an impediment to the emerging export industry. With regard to public expenditure management, there is an urgent need to introduce more expeditious procedures at the expenditure commitment level, in particular for the release of the domestic contribution to the investment costs, so as to enable

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[10] The authorities explained that they could not modify the accounting framework of the central bank to achieve full compliance with IAS, as per the recommendations of the safeguards assessment report, because this would require a change of the central bank law.

faster execution of donor-funded projects. Notwithstanding the progress made in 2001, further improvements are required in treasury accounting and in the monitoring of expenditure execution to permit a rapid assessment of the intrayear budgetary situation and speed up the closure of treasury accounts at year's end. While the staff is encouraged by the actions taken in recent weeks to repay a large part of domestic arrears, it is essential that procedures for repayment of VAT credits be thoroughly revamped, so as to avoid a future incurrence of arrears, which would damage the export sector.

58. **The actions taken with donor support to** counter **the worrisome decrease in school attendance and in the utilization of basic health services caused by the crisis in the first half of 2002 appear appropriate.** Donor-funded projects in the areas of basic nutrition and rural development have also played a role in alleviating the impact of the crisis on the most vulnerable groups.

59. **The budget for 2003, as prepared by the government, is consistent with the macroeconomic constraints.** It provides a margin for widening wage differentials; and, following extensive discussions with the donor community, it targets better the expenditures in priority sectors, funded by the debt relief under the HIPC Initiative. Appropriately, the deficit will be maintained within limits determined by the available external concessional financing, so that the banking system's resources can be channeled to support private sector recovery. On the revenue side, while noting the cut in customs duties on a number of inputs essential for the export sector and the reduction of the maximum tariff from 30 percent to 25 percent, the staff would underscore the need that tax revisions be undertaken in a comprehensive manner, in order to preserve total receipts. In the immediate future, the revenue impact of these measures needs to be offset by an increased effectiveness in tax administration, in order to maintain the overall revenue effort.

60. **Prospects for the balance of payments over the medium term are favorable,** provided that the export sector continues to benefit from inflows of foreign direct investment; for this to occur, improved public administration is essential. The level of the exchange rate appears broadly appropriate, as labor costs remain highly competitive, and the real effective appreciation of 2000 and 2001 has been partially reversed.

61. **The staff welcomes the decisions of the government to carry on with determination the restructuring and privatization of public enterprises.** Although difficult financial conditions and the unfavorable international environment have delayed the privatization of Air Madagascar, the restructuring of the company under foreign management should pave the way to its full privatization in the near term. It is also encouraging that the authorities have decided to open up the capital of the cotton company, HASYMA, which can play an important role in the vertical integration of the textile sector. It is important that management of the electricity company, JIRAMA, be strengthened in the period ahead with external assistance, and that the company be placed on a sound financial footing.

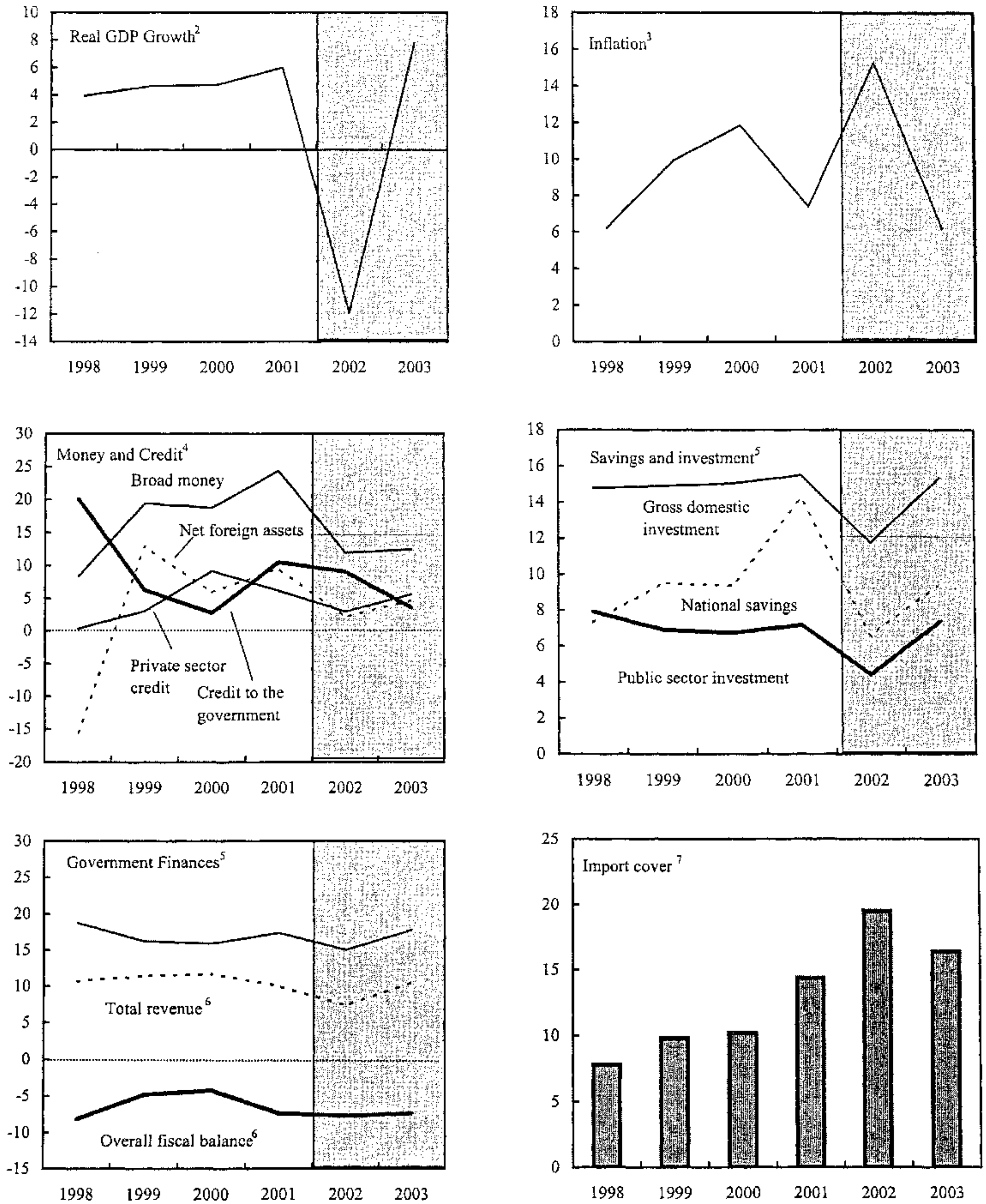
62. **The completion of the PRSP has been delayed by the political crisis.** The final version of the PRSP, expected to be completed by March 2003, will give emphasis to the need to improve governance at all levels of public administration as a means to promote

investment and growth. It is essential that the PRSP include a careful costing of the priority action programs and detailed monitoring mechanisms.

63. **In view of the satisfactory results achieved in 2001 under the program, the measures adopted to correct revenue** weaknesses, **and the steps taken so far in 2002 to improve tax administration and improve governance, the staff recommends that waivers be granted for the nonobservance of the end-December 2001 performance criteria on the net domestic assets of the central bank, domestic financing of the government, and tax revenue, and for the accumulation in early 2002 of arrears on external obligations.** It recommends that the second review under the PRGF arrangement be completed. The staff supports the authorities' requests for the extension of the three-year PRGF arrangement from end-February to end-November 2004, and for additional interim relief from the Fund under the enhanced HIPC Initiative to cover part of the debt-service obligations due to the Fund in 2003.

64. The staff recommends that the next Article IV consultation with Madagascar be held on the 24-month cycle, subject to the provisions of the decision on consultation cycles approved on July 15, 2002.

Figure 1. Madagascar: Selected Economic and Financial Indicators, 1998-2003[1]



Source: IMF, African Department.

[1]Shaded areas indicate projections.

[2]In percent.

[3]Percentage change in consumer prices based on traditional price index (yearly average).

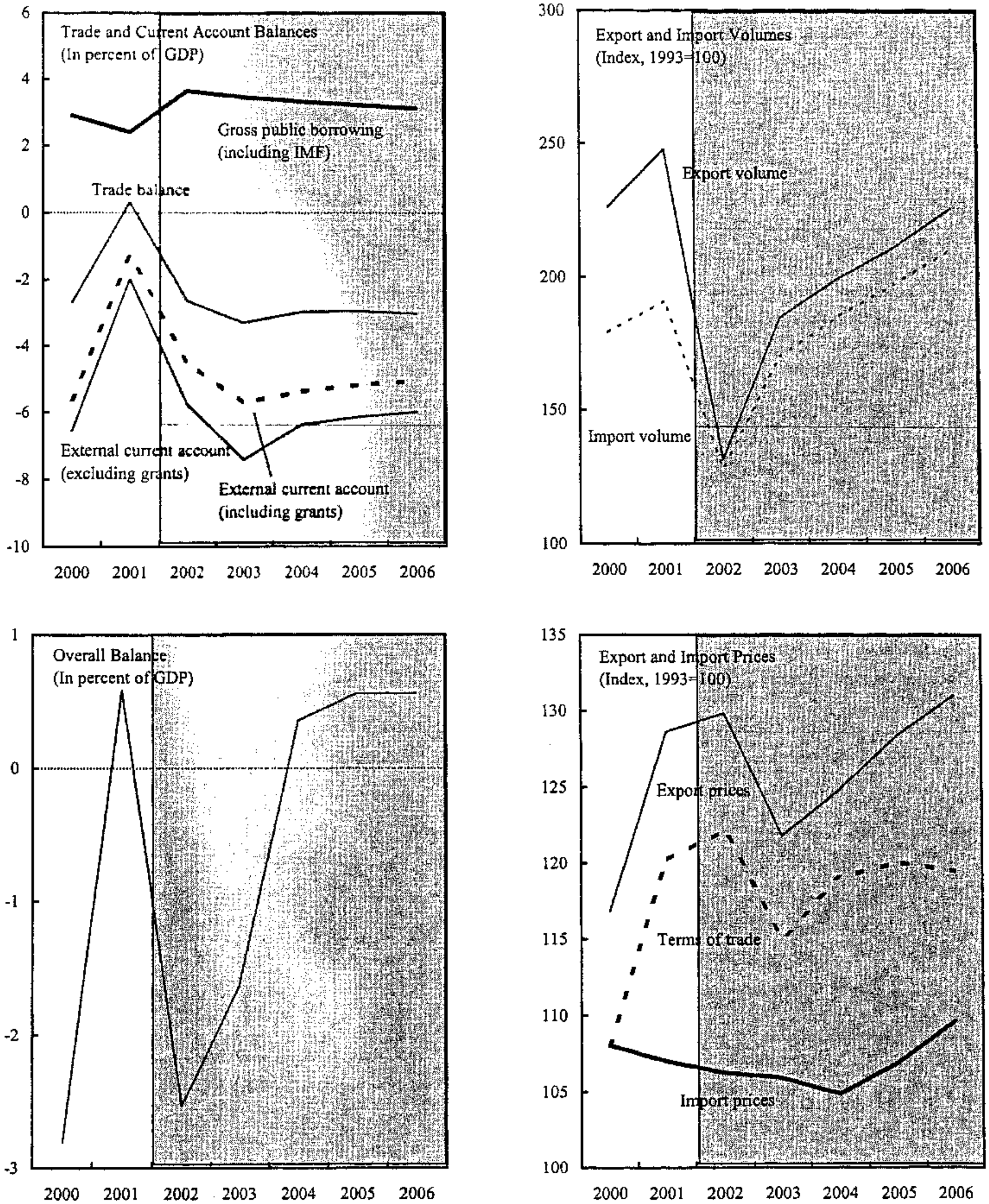
[4]In percent of beginning-of-period stock of broad money.

[5]In percentage of GDP.

[6]Excluding grants and the costs of structural reforms.

[7]International reserves, in weeks of imports of goods and nonfactor services.

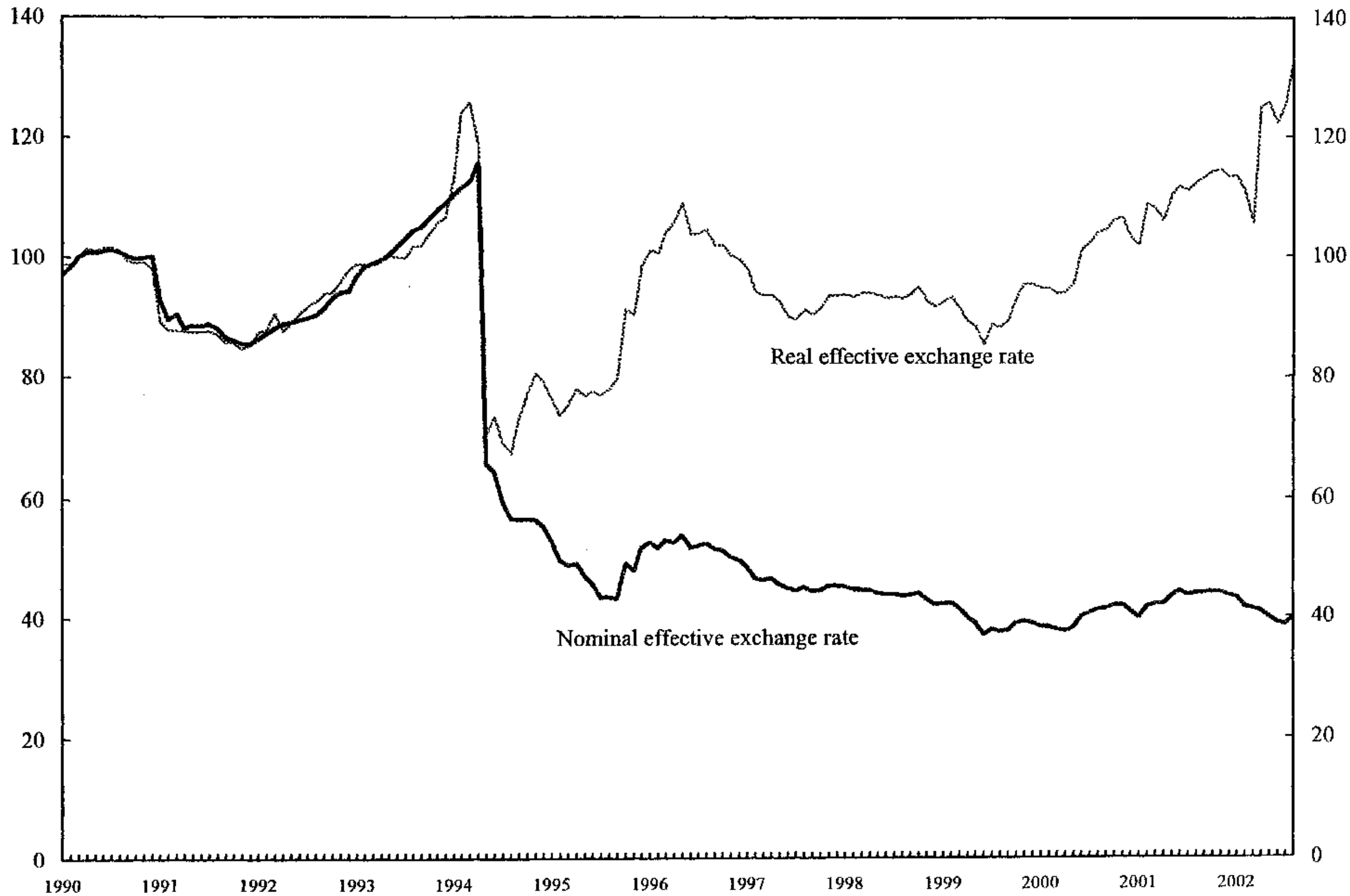
Figure 2. Madagascar: External Sector Developments and Prospects, 2000-06 [1]



Source: IMF, African Department.

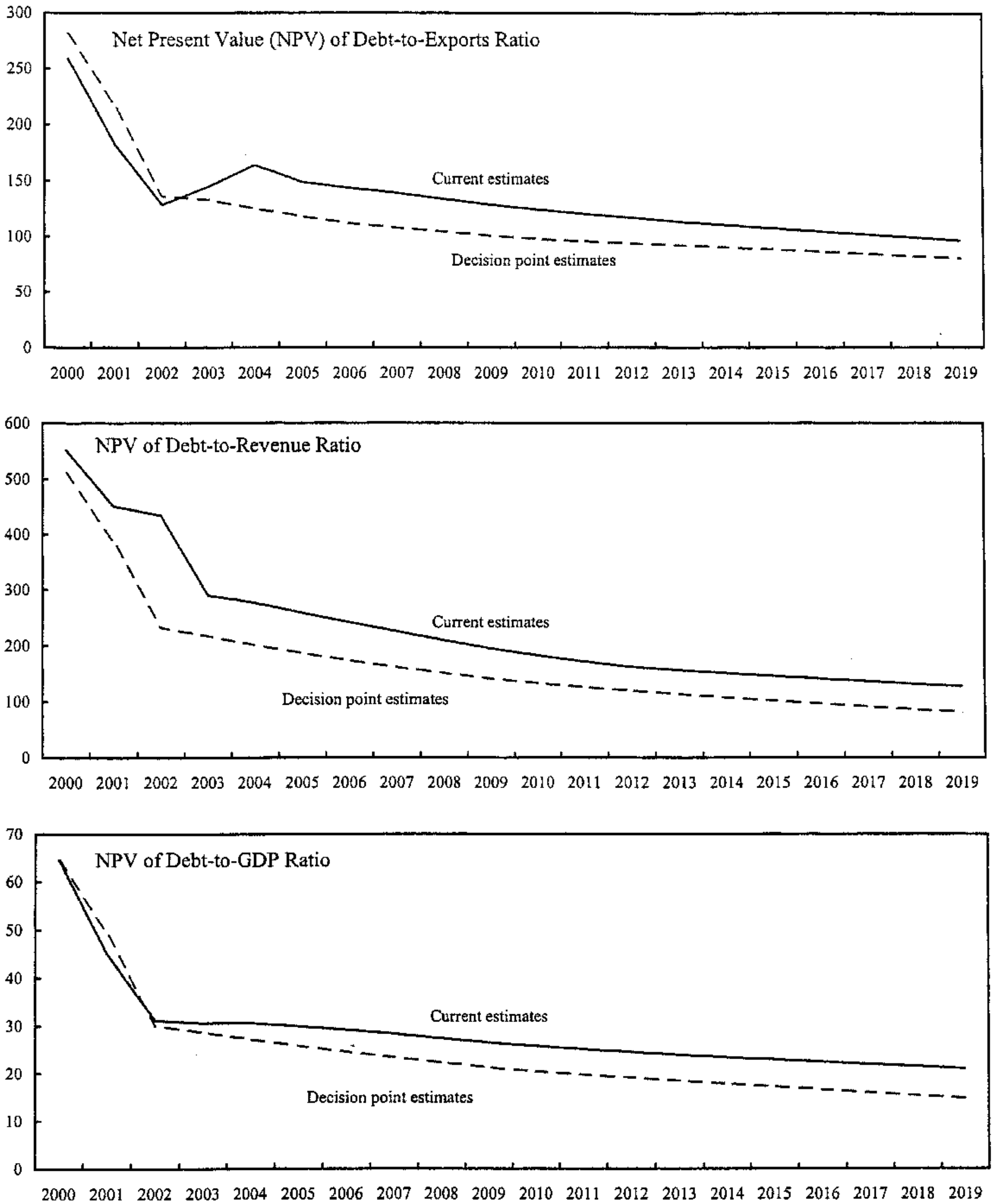
[1] Shaded area indicates projections.

Figure 3. Madagascar: Real and Nominal Exchange Rates, January 1990 - August 2002
(Average, 1990=100)



Source: IMF, Information Notice System.

Figure 4. Madagascar: Debt Sustainability Analysis, 2000-19



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

Table 1. Madagascar: Tentative Work Program Under The Proposed Revised PRGF Arrangement, 2002–04

Date	Action	Disbursement
October 2002	Second review mission under the PRGF arrangement, discussion of program for 2003, and 2002 Article IV consultation discussion.	
December 2002	Executive Board consideration of second review under the PRGF arrangement, and conclusion of the 2002 Article IV consultation.	SDR 11.347 million
February 2003	Mission to conduct the third review under the PRGF arrangement.	
April 2003	Executive Board consideration of the third review under the PRGF arrangement and of new annual program.	SDR 11.347 million
September 2003	Fourth review under the PRGF arrangement, 2003 Article IV consultation discussions, and discussion of program for 2004.	
November 2003	Executive Board consideration of the fourth review under the PRGF, and conclusion of the 2003 Article IV consultation.	SDR 11.347 million
February 2004	Mission to conduct the fifth review under the PRGF arrangement and discussion of program for 2004.	
April 2004	Executive Board consideration of fifth review under the PRGF arrangement. Expected completion point under the HIPC Initiative.	SDR 11.347 million
September 2004	Mission to conduct the sixth review under the PRGF.	
November 2004	Executive Board consideration of sixth review under PRGF, and conclusion of the Article IV consultation. Arrangement expires.	SDR 11.348 million.

Table 2. Madagascar: Selected Economic and Financial Indicators, 1997-2003 [1]

	1997	1998	1999	2000	2001		2002		2003	
					Rev. Prog.[2]	Act.	Orig. Proj.	Rev. Proj.	Orig. Proj.	Rev. Proj.
	(Annual percentage change, unless otherwise indicated)									
National accounts and prices										
Real GDP at market prices	3.7	3.9	4.7	4.8	6.7	6.0	4.8	-11.9	5.9	7.8
GDP deflator	7.3	8.4	9.8	7.1	7.4	9.0	4.8	15.4	3.0	3.8
Consumer price index										
Average	4.5	6.2	9.9	11.9	5.0	7.4	4.5	15.3	3.0	6.2
End of period	4.8	6.4	14.4	8.7	4.5	4.8	4.5	12.0	2.8	5.0
Money and credit (in percent of initial money stock)										
Net foreign assets, excluding long-term external liabilities	18.6	-15.6	12.9	5.9	9.7	9.5	...	2.1	...	4.7
Net domestic assets	1.9	24.1	7.7	12.2	5.9	15.4	...	9.3	...	7.9
Of which : Net domestic credit	3.4	20.5	9.3	12.1	7.6	16.6	...	12.0	...	9.2
Government	-3.3	20.1	6.3	2.8	4.8	10.5	...	9.1	...	3.6
Economy	6.7	0.4	3.1	9.2	2.8	6.1	...	3.0	...	5.6
Broad money (M3)	19.8	8.4	19.5	18.8	16.2	24.4	...	11.9	...	12.5
Velocity of money (GDP/end-of-period M3)	4.7	4.9	4.7	4.4	4.4	4.1	...	3.7	...	3.7
External sector (in terms of SDRs)										
Exports, f.o.b.	1.7	4.3	11.3	47.6	14.3	20.6	7.4	-46.4	11.3	31.8
Imports, c.i.f.	-3.7	0.0	7.4	29.0	14.6	5.5	5.2	-33.4	3.2	32.1
Terms of trade (deterioration -) [3]	5.6	5.9	-24.0	8.1	8.0	11.2	0.3	1.6	-0.1	-5.9
Nominal effective exchange rate [4]										
Average	-12.1	-3.7	-10.4	1.3	...	8.1	...	-5.6	...	...
End of period	-8.8	-6.9	-7.5	4.9	...	7.0	...	-11.4	...	...
Real effective exchange rate [4]										
Average	-10.1	0.8	-2.7	10.1	...	10.4	...	7.2	...	...
End of period	-6.2	-1.9	4.0	9.6	...	9.6	...	10.6	...	...
	(In percent of GDP)									
National accounts										
Gross domestic investment	12.8	14.8	14.9	15.0	18.3	15.5	18.8	11.1	20.0	15.2
Public sector	6.5	7.9	6.9	6.7	10.1	7.2	10.8	3.7	11.7	7.2
Private sector (including public enterprises)	6.3	6.9	8.0	8.3	8.3	8.3	7.9	7.3	8.3	8.0
Gross national savings	7.3	7.3	9.5	9.4	12.8	14.2	11.2	6.6	13.3	9.5
Public sector	1.1	0.8	3.1	3.4	3.4	0.5	3.6	-1.9	5.3	1.9
Private sector (including public enterprises)	6.2	6.5	6.5	6.0	9.4	13.7	7.6	8.5	8.0	7.6
Gross domestic savings	4.7	7.0	7.2	7.8	...	12.3	...	5.2	...	7.3
Central government financial operations										
Total revenue	9.7	10.6	11.4	11.7	11.9	10.0	...	7.3	13.3	10.5
Of which : tax revenue	9.4	9.8	11.0	11.3	11.5	9.6	...	7.0	12.9	10.2
Total expenditure	17.4	18.8	16.2	15.9	20.1	17.3	...	15.0	21.6	17.8
Of which: interest obligations	3.0	2.7	2.1	2.3	2.0	2.0	...	2.1	1.9	1.8
noninterest current expenditures	6.9	7.4	7.2	6.9	7.9	7.9	...	7.0	7.8	8.2
capital expenditure	6.5	8.2	6.9	6.7	10.0	7.2	...	3.7	11.7	7.2
Net balance of structural reforms	-0.7	0.0	-0.1	-2.2	-1.7	-0.7	...	0.0	-0.5	0.0
Overall balance (commitment basis; including restructuring operations)										
Including grants	-2.4	-5.8	-2.8	-2.8	-5.4	-4.3	...	-4.9	-3.4	-4.1
Excluding grants	-7.7	-9.3	-6.4	-6.4	-9.9	-8.1	...	-7.7	-8.8	-7.4
Total balance (cash basis; including restructuring operations) [5]	-4.4	-5.4	-4.8	-3.3	-5.8	-4.4	...	-5.5	-3.4	-5.1

Table 2. Madagascar: Selected Economic and Financial Indicators, 1997-2003 (concluded)

	1997	1998	1999	2000	2001 Rev. Prog.[2]	2001 Act.	2002 Orig. Proj.	2002 Rev. Proj.	2003 Orig. Proj.	2003 Rev. Proj.
	(In percent of GDP)									
External current account										
Excluding official transfers	-7.8	-7.9	-6.3	-6.5	-7.2	-2.0	-8.5	-5.8	-8.0	-7.4
Including current official transfers	-5.5	-7.4	-5.4	-5.7	-5.6	-1.3	-7.5	-4.5	-6.7	-5.7
Net present value (NPV) of external debt [6 7]	...	...	55.3	55.4	50.1	48.6	46.7	51.6	45.3	48.9
	(In percent of exports of goods and services)									
Scheduled external debt service [6]										
Before debt relief	27.2	26.4	17.6	13.2	12.0	10.9	12.6	20.3	15.7	15.1
After debt relief [5 7 8]	19.3	20.0	11.4	6.5	4.8	3.7	4.9	7.1	5.5	5.8
	(In units indicated)									
Gross official reserves (in millions of SDRs)	208.4	121.8	165.5	218.7	298.9	317.5	346.2	296.1	390.7	336.9
In weeks of imports of goods and nonfactor services	14.1	7.8	9.8	10.2	12.3	14.4	13.2	19.5	14.6	16.4
Exchange rates (period average)										
Malagasy francs per SDR	7,016.1	7,381.7	8,585.8	8,934.0	...	8,385.8	...	...	...	...
Nominal GDP at market prices (in billions of Malagasy francs)	18,051	20,343	23,379	26,242	30,084	30,334	33,041	30,842	35,322	34,506
GDP per capita (U.S. dollars)	251	257	248	251	285	290	307	295	322	321

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

[1] Data may not add up due to rounding.

[2] EBS/01/193, 11/21/01.

[3] Based on 1993 trade weights.

[4] Data reported for 2002 are based on the seven months to July 2002.

[5] Including grants.

[6] Reflects Paris Club flow rescheduling on Naples terms obtained for the period January 1997 - November 2000 and assumes similar terms for non-Paris Club creditors.

[7] Provisional. NPVs of debt from debt sustainability analysis (DSA), which assumes a stock-of-debt operation at end-1999.

[8] For 2001-03, the debt service is calculated assuming the full application of traditional debt-relief mechanisms, as well as HIPC Initiative relief.

Table 3. Madagascar: Quarterly Financial Operations of the Central Government, 2002-03
(In billions of Malagasy francs, unless otherwise indicated; cumulative)

	2002				2003			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	Prel.	Prel.	Prel.	Proj.	Projections			
Total revenue and grants	540.3	992.7	1,710.1	3,115.1	1,005.8	2,415.9	3,442.0	4,707.9
Total revenue	461.6	857.2	1,508.7	2,250.6	783.0	1,752.9	2,552.5	3,617.0
Budgetary revenue	461.6	857.2	1,508.7	2,250.6	783.0	1,752.9	2,552.5	3,617.0
Of which: tax revenue	424.3	807.9	1,449.6	2,162.3	755.0	1,700.0	2,480.0	3,509.0
Capital revenue	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Grants	78.7	135.5	201.3	864.5	222.8	663.0	889.5	1,090.9
Current grants	69.7	117.5	176.3	498.5	74.8	367.0	445.5	498.9
Of which: HIPC assistance	50.8	86.5	141.1	179.1	63.1	103.0	164.8	205.9
Project grants	9.0	18.0	25.0	366.0	148.0	296.0	444.0	592.0
Total expenditure	667.5	1,566.0	2,383.3	4,622.7	1,478.6	3,160.4	4,664.1	6,154.7
Current expenditure	552.0	1,322.8	1,958.2	3,250.7	879.7	1,799.7	2,671.3	3,547.9
Budgetary expenditure	331.3	901.2	1,481.6	2,823.4	815.9	1,696.1	2,541.2	3,444.7
Personnel [1]	201.9	544.3	925.5	1,399.4	465.3	930.7	1,396.0	1,815.9
Of which: HIPC financed	0.0	0.0	7.0	71.4	29.9	59.9	89.8	119.8
Other noninterest expenditure	45.1	119.6	218.7	771.2	232.7	464.6	733.3	1,024.3
Of which: HIPC financed	0.0	0.0	0.0	123.5	23.9	51.3	89.8	119.7
Foreign interest obligations	68.2	191.8	243.0	391.0	66.1	199.6	262.6	402.7
Domestic interest obligations	16.2	45.5	94.5	261.8	51.8	101.2	149.4	201.8
Treasury operations (net) [2]	220.5	373.0	411.6	305.1	63.0	102.0	92.7	65.0
Emergency expenditure	0.0	48.2	64.0	119.0	0.0	0.0	35.0	35.0
Counterpart funds-financed operations	0.2	0.4	1.0	3.2	0.8	1.6	2.4	3.2
Capital expenditure	115.5	243.2	425.1	1,149.0	543.4	1,249.6	1,881.7	2,495.7
Domestic financing	7.7	15.7	85.6	242.0	120.0	400.0	600.0	800.0
Foreign financing	107.8	227.5	339.5	907.0	423.4	849.6	1,281.7	1,695.7
Of which: HIPC financed	0.0	0.0	0.0	123.2	30.4	63.6	102.7	123.7
Government on-lending to public enterprises	0.0	0.0	0.0	223.0	55.6	111.1	111.1	111.1
Overall balance (commitment basis, excluding the cost of structural reforms)								
Including grants	-127.3	-573.3	-673.3	-1,507.6	-472.8	-744.5	-1,222.1	-1,446.8
Excluding grants	-206.0	-708.8	-874.6	-2,372.1	-695.6	-1,407.5	-2,111.6	-2,537.7
Net balance of structural reforms	3.0	4.2	5.8	9.5	-7.0	-16.0	-19.0	-17.1
Exceptional revenue	3.0	4.2	5.8	9.5	3.0	4.0	6.0	10.0
Cost of structural reforms	0.0	0.0	0.0	0.0	10.0	20.0	25.0	27.1
Overall balance (commitment basis, including the cost of structural reforms)								
Including grants	-124.3	-569.1	-667.5	-1,498.1	-479.8	-760.5	-1,241.1	-1,463.9
Excluding grants	-203.0	-704.6	-868.8	-2,362.6	-702.6	-1,423.5	-2,130.6	-2,554.8
Domestic balance [3]	-27.0	-285.3	-286.3	-1,064.6	-213.1	-374.3	-586.3	-456.4
Change in arrears [4]	-55.3	-73.9	-215.4	-196.7	-81.3	-147.5	-203.8	-300.0
Total overall balance (cash basis, including grants)	-179.6	-643.0	-882.9	-1,694.8	-561.1	-908.0	-1,444.9	-1,763.9
Financing	179.6	643.0	882.9	1,694.8	561.1	908.0	1,444.9	1,763.9
Foreign (net)	276.8	438.0	457.4	967.3	297.0	806.7	1,118.5	1,306.7
Drawings	281.1	391.8	564.1	1,096.7	348.5	698.5	943.5	1,188.5
Budget	182.3	182.3	249.6	678.7	103.5	208.5	208.5	208.5
Projects	98.8	209.5	314.5	418.0	245.0	490.0	735.0	980.0
Amortization due	-173.9	-322.0	-485.3	-640.6	-190.2	-343.5	-462.1	-660.6
Change in external arrears [5]	38.7	103.1	0.0	0.0	0.0	0.0	0.0	0.0
Debt relief	131.0	265.1	378.5	511.2	138.7	274.7	324.3	466.0
Of which : current maturities	107.2	183.8	277.2	352.1	113.2	189.8	229.2	308.8
HIPC assistance	23.8	81.2	101.3	159.0	25.4	84.9	95.1	157.2
Financing gap (exceptional)	0.0	0.0	0.0	0.0	0.0	177.0	312.8	312.8
Domestic (net)	-103.4	189.3	379.0	678.2	167.7	-16.6	195.8	324.3
Banking system	-55.7	232.3	417.3	651.6	162.7	-76.6	110.8	212.7
Nonbanking system	-52.7	-53.0	-53.3	7.3	0.0	50.0	70.0	91.6
Treasury correspondent accounts (net)	5.0	10.0	15.0	19.3	5.0	10.0	15.0	20.0
Privatization receipts	6.2	15.8	46.5	49.4	96.4	117.8	130.6	132.9
Memorandum items:								
Domestic financing of the government	-157.5	121.2	195.1	530.9	182.8	-46.3	122.6	157.2
Financing gap	0.0	0.0	0.0	0.0	0.0	177.0	312.8	312.8
Financing gap (in millions of U.S. dollars)	0.0	0.0	0.0	0.0	0.0	25.3	44.1	44.1

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

[1] Personnel expenditures in 2002 were much lower than in the budget as the payment of a number of indemnities and allowances was suspended because of the revenue shortfall.

[2] Includes annexed budgets of quasi-public entities, including port authorities, the post office, government printing office, and civil service retirement funds. Beginning in 2002 net correspondent account balances are classified as domestic financing.

[3] Overall balance, excluding grants, foreign-financed capital expendiures, and foreign interest payments.

[4] Representing the difference between expenditure committed and actual payments.

[5] Bilateral agreements on debt with non-Paris Club creditors, most of which is in arrears, were initially assumed to be finalized in 2001; however, such reschedulings are materializing at a slower pace than envisaged. For 2001, arrears were rescheduled with the Saudi Fund for Development and a commercial creditor, Itochu Bank (Hong Kong SAR).

Table 4. Madagascar: Central Government Accounts, 1997-2003
(In billions of Malagasy francs, unless otherwise indicated)

	1997	1998	1999	2000	2001 Rev. Prog.	2001 Act.	2002 Rev. Prog.	2002 Est.	2003 Proj.
Total revenue and grants	2,703.2	2,872.6	3,509.9	4,014.4	4,930.9	4,190.6	5,637.0	3,115.1	4,707.9
Total revenue	1,746.8	2,164.8	2,667.4	3,067.7	3,572.8	3,029.0	4,133.6	2,250.6	3,617.0
Budgetary revenue	1,746.8	2,076.8	2,667.4	3,067.7	3,572.8	3,029.0	4,133.6	2,250.6	3,617.0
Of which: tax revenue	1,687.9	1,984.4	2,580.1	2,972.1	3,470.0	2,906.4	4,040.0	2,162.3	3,509.0
Grants	956.5	707.8	842.5	946.7	1,358.1	1,161.6	1,503.4	864.5	1,090.9
Current grants	377.7	59.8	171.9	178.9	466.2	427.7	308.4	498.5	498.9
Of which: HIPC assistance [1]	...	...	...	...	157.9	157.9	162.9	179.1	205.9
Project grants	578.8	648.0	670.6	767.8	891.9	733.9	1,195.0	366.0	592.0
Total expenditure	3,137.1	3,819.3	3,790.9	4,168.6	6,035.7	5,262.6	7,021.4	4,622.7	6,154.7
Current expenditure	1,960.2	2,146.1	2,175.0	2,402.5	3,040.2	3,081.7	3,329.7	3,250.7	3,547.9
Budgetary expenditure	1,801.6	2,052.1	2,172.4	2,416.5	2,970.2	3,001.0	3,269.5	2,823.4	3,444.7
Personnel [2]	669.6	826.4	1,000.6	1,042.4	1,336.7	1,337.6	1,549.0	1,399.4	1,815.9
Of which: HIPC financed	...	...	...	...	71.0	71.0	71.4	71.4	119.8
Other noninterest expenditure	583.0	671.9	679.0	761.8	1,037.7	1,071.5	1,126.3	771.2	1,024.3
Of which: HIPC financed	...	...	...	...	126.0	95.3	123.5	123.5	119.7
Foreign interest obligations	503.5	466.5	325.0	371.2	349.1	349.1	386.8	391.0	402.7
Domestic interest obligations	45.4	87.3	167.8	241.1	246.7	242.8	207.4	261.8	201.8
Treasury operations (net) [3]	120.1	94.0	2.6	-56.5	45.0	54.3	30.0	305.1	65.0
Emergency expenditure [4]	38.5	0.0	0.0	40.6	25.0	25.0	27.0	119.0	35.0
Of which: elections	...	...	...	...	...	...	...	55.0	35.0
Counterpart funds-financed operations	...	...	...	2.0	0.7	1.4	3.2	3.2	3.2
Capital expenditure	1,176.9	1,673.1	1,615.9	1,766.1	2,995.5	2,180.9	3,691.7	1,149.0	2,495.7
Domestic financing	274.5	465.6	429.6	581.2	1,175.0	942.3	1,203.5	242.0	800.0
Foreign financing	902.0	1,207.5	1,186.3	1,184.9	1,820.5	1,238.6	2,428.2	907.0	1,695.7
Of which: HIPC financed	...	...	...	...	124.2	131.0	123.2	123.2	123.7
Government on-lending									
AIR MAD	...	...	...	...	...	...	...	67.0	41.1
RNCFM	...	...	...	...	...	...	...	55.0	32.0
SIRAMA	...	...	...	...	...	...	...	0.0	28.0
HASYMA	...	...	...	...	...	...	...	13.0	10.0
JIRAMA	...	...	...	...	...	...	...	88.0	0.0
Overall balance (commitment basis, excluding the cost of structural reforms)									
Including grants	-433.9	-946.7	-281.0	-154.2	-1,104.8	-1,072.0	-1,384.4	-1,507.6	-1,446.8
Excluding grants	-1,390.4	-1,654.5	-1,123.5	-1,100.9	-2,462.9	-2,233.6	-2,887.8	-2,372.1	-2,537.7
Net cost of structural reforms [5]	0.0	-236.7	-369.7	-582.7	-522.9	-223.1	-319.3	9.5	-17.1
Exceptional revenue	0.0	0.0	45.6	17.7	8.0	11.5	15.0	9.5	10.0
Cost of structural reforms	0.0	236.7	415.3	600.4	530.9	234.6	334.3	0.0	27.1
Overall balance (commitment basis, including the cost of structural reforms)									
Including grants	-433.9	-1,183.4	-650.7	-737.0	-1,788	-1,295.1	-1,703.7	-1,498.1	-1,463.9
Excluding grants	-1,390.4	-1,891.2	-1,493.2	-1,683.7	-2,948	-2,456.7	-3,207.1	-2,362.6	-2,554.8
Domestic balance [6]	15.2	-217.1	18.1	-127.6	-724	-868.9	-392.1	-1064.6	-456.4
Change in arrears	-139.4	-101.8	67.6	-135.9	-115.0	-27.0	-92.2	-196.7	-300.0
Total overall balance (cash basis, including grants)	-573.3	-1,285.2	-583.1	-872.8	-1742.7	-1,322.0	-1,795.9	-1,694.8	-1,763.9
Financing	573.3	1,285.3	583.1	872.8	1,742.7	1,322.0	1,795.9	1,694.8	1,763.9
Foreign (net)	692.3	379.4	284.9	704.7	1,165.5	635.6	1,418.8	967.3	1,306.7
Drawings	1,029.3	672.5	515.7	802.4	1,301.3	723.4	1,546.3	1,096.7	1,188.5
Budget	...	...	...	385.3	496.9	218.7	436.3	678.7	208.5
Of which: World Bank EERC	...	...	...	...	...	...	...	134.0	208.5
Projects	...	...	...	417.1	804.4	504.7	1,110.0	418.0	980.0
Amortization due	-508.9	-662.1	-607.5	-621.5	-581.0	-581.0	-621.7	-640.6	-660.6
Change in external arrears	-5,459.7	88.6	27.6	-49.5	-68.2	-68.2	0.0	0.0	0.0
External debt relief	5,631.7	280.5	349.1	573.2	513.4	561.3	339.1	511.2	466.0
Of which: HIPC assistance [7]	...	...	...	...	151.0	151.0	155.1	159.0	157.2
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	312.8
(in millions of U.S. dollars)	...	...	...	...	...	...	...	0.0	44.1
Domestic (net)	-119.0	901.5	246.4	121.9	377.4	580.9	80.8	678.2	324.3
Banking system	-146.0	741.2	167.1	3.1	261.2	468.4	-38.0	651.6	212.7
Nonbanking system	27.0	160.3	79.3	118.8	116.1	112.5	118.8	7.3	91.6
Treasury correspondent accounts (net) [3]	...	...	...	...	...	...	0.0	19.3	20.0
Privatization receipts	0.0	4.4	51.8	46.3	199.8	104.1	296.3	49.4	132.9
Of which: TELMA	...	...	...	...	...	...	...	...	84.0
Memorandum items:									
Domestic financing of the government	...	...	...	...	...	658.1	322.9	530.9	157.2
Total HIPC debt relief	...	...	...	...	308.9	297.3	318.0	318.1	363.2

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

[1] Interim HIPC Initiative assistance of multilateral financial institutions for 2001-03.

[2] Personnel expenditures in 2002 have been much lower than in the budget as the payment of a number of indemnities and allowances was suspended because of the revenue shortfall.

[3] Includes annexed budgets of quasi-public entities, including port authorities, the post office, government printing office, civil service retirement funds, and correspondent accounts of local authorities, until 2002, when net correspondent account balances are classied as domestic financing.

[4] For 2000, the government budgeted FMG 69 billion to address exceptional developments related to the resurgence of a cholera epidemic and the devastating effects of three cyclones early in the year.

[5] The net cost of structural reforms comprise (i) as receipts, loan recovery by the debt-recovery unit that holds the nonperforming loans of the two (former) public banks (BFV and BTM) after their assets have been financially restructured; and (ii) as expenditures, those related to civil service reform (i.e., training, bonuses, and wage decompression); to the upgrading of pay and equipment in the justice services; to privatization (severance pay, administrative costs, transfers to the regional development fund that provides grants and concessional loans for basic social infrastructure purposes or to employees affected by privatization, and indemnization payments to formerly expropriated owners); and to the capital transfers for the asset restructuring at the two insolvent banks (BFV and BTM).

[6] Total revenue minus expenditure, excluding foreign interest payments and foreign-financed capital expenditure.

[7] Interim HIPC Initiative assistance provided through Paris Club flow rescheduling on Cologne terms for 2001-03.

Table 5. Madagascar: Central Government Ratios, 1997-2003
(In percent of GDP, unless otherwise indicated)

	1997	1998	1999	2000	2001		2002		2003
					Rev. Prog.	Act.	Rev. Prog.	Est.	Proj.
Total revenue and grants	15.0	14.1	15.0	15.3	16.4	13.8	17.1	10.1	13.6
Total revenue	9.7	10.6	11.4	11.7	11.9	10.0	12.5	7.3	10.5
Of which: tax revenue	9.4	9.8	11.0	11.3	11.5	9.6	12.2	7.0	10.2
Grants	5.3	3.5	3.6	3.6	4.5	3.8	4.6	2.8	3.2
Current grants	2.1	0.3	0.7	0.7	1.5	1.4	0.9	1.6	1.4
Of which: HIPC assistance [1]	...	...	...	...	0.5	0.5	0.5	0.6	0.6
Project grants	3.2	3.2	2.9	2.9	3.0	2.4	3.6	1.2	1.7
Total expenditures	17.4	18.8	16.2	15.9	20.1	17.3	21.3	15.0	17.8
Current expenditure	10.9	10.5	9.3	9.2	10.1	10.2	10.1	10.5	10.3
Noninterest expenditure	6.9	7.4	7.2	6.9	7.9	7.9	8.1	7.0	8.2
Personnel	3.7	4.1	4.3	4.0	4.4	4.4	4.7	4.5	5.3
Of which: HIPC financed	...	...	...	...	0.2	0.2	0.2	0.2	0.3
Other noninterest expenditure	3.2	3.3	2.9	2.9	3.4	3.5	3.4	2.5	3.0
Of which: HIPC financed	...	...	...	...	0.4	0.3	0.4	0.4	0.3
Interest obligations	3.0	2.7	2.1	2.3	2.0	2.0	1.8	2.1	1.8
Treasury operations [2]	0.7	0.5	0.2	-0.2	0.1	0.2	0.1	1.0	0.2
Emergency expenditures [3]	0.2	0.0	0.0	0.2	0.1	0.1	0.1	0.4	0.1
Of which: elections	...	...	...	...	...	...	...	0.2	0.1
Capital expenditure	6.5	8.2	6.9	6.7	10.0	7.2	11.2	3.7	7.2
Domestically financed expenditure	1.5	2.3	1.8	2.2	3.9	3.1	3.6	0.8	2.3
Foreign-financed expenditure	5.0	5.9	5.1	4.5	6.1	4.1	7.3	2.9	4.9
Of which: HIPC financed	...	...	...	...		0.4	0.4	0.4	0.4
Government on-lending									
AIR MAD	...	...	...	...	...	...	...	0.2	0.1
RNCFM	...	...	...	...	...	...	...	0.2	0.1
SIRAMA	...	...	...	...	...	...	...	0.0	0.1
HASYMA	...	...	...	...	...	...	...	0.0	0.0
JIRAMA	...	...	...	...	...	...	...	0.3	0.0
Overall balance (commitment basis, excluding the cost of structural reforms)									
Including grants	-2.4	-4.7	-1.2	-0.6	-3.7	-3.5	-4.2	-4.9	-4.2
Excluding grants	-7.7	-8.1	-4.8	-4.2	-8.2	-7.4	-8.7	-7.7	-7.4
Net cost of structural reforms [4]	0.0	-1.2	-1.6	-2.2	-1.7	-0.7	-1.0	0.0	0.0
Exceptional revenue	0.0	0.0	0.2	0.1	0.0	0.0	0.0	0.0	0.0
Cost of structural reforms	0.0	1.2	1.8	2.3	1.8	0.8	1.0	0.0	0.1
Overall balance (commitment basis, including the cost of structural reforms)									
Including grants	-2.4	-5.8	-2.8	-2.8	-5.4	-4.3	-5.2	-4.9	-4.1
Excluding grants	-7.7	-9.3	-6.4	-6.4	-9.9	-8.1	-9.7	-7.7	-7.4
Domestic balance [5]	0.1	-1.1	0.1	-0.5	-2.7	-2.9	-1.2	-3.5	-1.3
Change in arrears	-0.8	-0.5	0.3	-0.5	-0.4	-0.1	-0.3	-0.6	-0.9
Total overall balance (cash basis, including grants)	-3.2	-6.3	-2.5	-3.3	-5.8	-4.4	-5.4	-5.5	-5.1
Financing	3.2	6.3	2.5	3.3	5.8	4.4	5.4	5.5	5.1
Foreign (net)	3.8	1.9	1.2	2.7	3.9	2.1	4.3	3.1	3.8
Drawings	5.7	3.3	2.2	3.1	4.3	2.4	4.7	3.6	3.4
Budget	...	...	...	1.5	1.7	0.7	1.3	2.2	0.6
Of which: World Bank EERC	...	...	...	...	...	...	...	0.4	0.6
Projects	...	...	...	1.6	2.7	1.7	3.4	1.4	2.8
Amortization due	-2.8	-3.3	-2.6	-2.4	-1.9	-1.9	-1.9	-2.1	-1.9
Change in external arrears	-30.2	0.4	0.1	-0.2	-0.2	-0.2	0.0	0.0	0.0
External debt relief	31.2	1.4	1.5	2.2	1.7	1.9	1.0	1.7	1.4
Of which: HIPC assistance [6]	...	...	...	...	0.5	0.5	0.5	0.5	0.5
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.9
Domestic (net)	-0.7	4.4	1.1	0.5	1.3	1.9	0.2	2.2	0.9
Of which: banking system	-0.3	2.0	0.6	0.0	0.9	1.5	-0.1	2.1	0.6
Privatization receipts	0.0	0.0	0.2	0.2	0.7	0.3	0.9	0.2	0.4
Memorandum items:									
Total HIPC debt relief	...	...	...	...	1.0	1.0	1.0	1.0	1.1
Education expenditure, after HIPC	2.2	2.5	3.0	2.9	3.3	...	3.8	...	...
Health expenditure, after HIPC	1.0	1.0	1.2	1.8	1.9	...	2.1	...	...
Nominal GDP (in billions of Malagasy francs)	18,051	20,343	23,379	26,242	30,084	30,334	33,041	30,842	34,506

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

[1] Interim HIPC assistance of multilateral financial institutions for 2001-03.

[2] Includes annexed budgets of quasi-public entities, including port authorities, the post office, government printing office, civil service retirement funds, and correspondent accounts of local authorities.

[3] For 2000, the government budgetized FMG 69 billion to address exceptional developments related to the resurgence of a cholera epidemic and the devastating effects of three cyclones early in the year.

[4] The net cost of structural reforms comprise (i) as receipts, loan recovery by the debt-recovery unit that holds the nonperforming loans of the two (former) public banks (BFV and BTM) after their assets have been financially restructured; and (ii) as expenditures, those related to civil service reform (i.e., training, bonuses, and wage decompression); to the upgrading of pay and equipment in the justice services; to privatization (severance pay, administrative costs, transfers to the the regional development fund that provides grants and concessional loans for basic social infrastructure purposes or to employees affected by privatization, and indemnization payments to formerly expropriated owners); and to the capital transfers for the asset restructuring at the two insolvent banks (BFV and BTM).

[5] Overall balance, excluding grants, foreign-financed capital expenditures and foreign interest payments.

[6] Interim HIPC assistance provided through Paris Club flow rescheduling on Cologne terms for 2001-03.

Table 6. Madagascar: Monetary Survey, 2000-2003

	2000	2001			2002					2003			
	Dec.	Dec.			Mar.		Jun	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.
	Act.	Prog.	Rev. Prog.	Act.	Prog.	Prov.	Prov.	Prel.	Prog.	Prog.	Prog.	Prog.	Prog.
	(In billions of Malagasy francs; end of period)												
Net foreign assets	2,006.3	2,544.4	2,582.5	2,571.1	2,752.1	2,669.7	2,670.0	2,295.4	2,726.3	2,747.3	2,834.5	3,061.9	3,114.6
Central bank	1,170.5	1,872.2	1,616.9	1,787.7	1,892.9	1,746.2	1,693.6	1,275.7	1,658.1	1,571.9	1,595.4	1,851.5	1,981.8
Commercial banks	835.9	672.2	965.6	783.5	859.2	923.5	976.3	1,019.7	1,068.2	1,175.4	1,239.1	1,210.5	1,132.7
Long-term foreign liabilities	-229.3	-214.9	-198.7	-264.2	-196.8	-235.2	-245.0	-226.3	-226.6	-230.0	-233.5	-236.9	-240.3
Central bank	-167.5	-165.4	-149.5	-149.0	-147.6	-155.5	-155.5	-161.5	-161.7	-164.2	-166.6	-169.1	-171.5
Commercial banks	-61.7	-49.4	-49.3	-115.2	-49.3	-79.7	-89.5	-64.8	-64.9	-65.9	-66.9	-67.9	-68.8
Net domestic assets	4,139.8	3,715.9	4,491.6	5,050.7	4,375.3	4,855.0	5,134.8	5,219.3	5,733.1	6,021.6	5,895.2	6,199.3	6,383.6
Net credit to government	1,856.5	1,372.6	2,143.1	2,477.1	2,114.8	2,429.8	2,713.2	2,845.3	3,143.6	3,684.5	3,466.1	3,668.7	3,791.5
Net claims on government 1/	1,563.3	1,179.6	1,824.5	2,047.8	1,792.4	1,991.7	2,279.6	2,414.8	2,710.2	3,231.6	3,000.6	3,196.4	3,306.6
Central bank 1/	1,162.7	628.8	930.1	1,207.8	919.4	1,078.6	1,377.0	1,567.4	1,870.2	2,228.9	2,160.6	2,356.4	2,466.6
Commercial banks	400.6	550.7	894.4	840.0	873.0	913.1	902.6	847.4	840.0	1,002.7	840.0	840.0	840.0
Other claims	293.2	193.0	318.6	429.2	322.4	438.2	433.6	430.5	433.4	452.9	465.5	472.3	484.9
Credit to the economy	2,415.0	2,764.6	2,578.5	2,778.3	2,503.8	2,884.5	2,717.6	2,681.2	2,995.5	2,762.7	2,882.4	3,012.2	3,107.8
Central bank	111.2	15.8	127.0	276.4	256.4	361.7	367.0	366.3	366.3	15.9	15.9	15.9	15.9
Commercial banks	2,303.3	2,604.6	2,451.4	2,500.8	2,247.2	2,519.1	2,350.6	2,311.8	2,629.0	2,743.8	2,866.4	2,993.3	3,091.7
Other claims	0.5	144.2	0.1	1.2	0.1	3.6	0.0	3.0	0.1	3.0	0.1	3.0	0.1
Other items (net)	-131.8	-421.3	-229.9	-204.7	-243.3	-459.3	-296.0	-307.1	-406.0	-425.7	-453.4	-481.6	-515.7
Foreign currency adjustment	84.6	42.9	104.7	55.4	41.2	-48.2	-30.0	4.4	-94.4	-124.4	-152.0	-180.3	-214.4
Central bank	190.0	15.4	134.9	166.0	203.0	82.0	183.0	170.9	170.9	170.9	170.9	170.9	170.9
Commercial banks	-406.4	-479.6	-469.5	-426.1	-487.5	-493.1	-448.9	-482.4	-482.4	-472.2	-472.2	-472.2	-472.2
Broad money (M3)	5,916.8	6,045.5	6,875.4	7,357.7	6,930.5	7,289.5	7,559.8	7,288.5	8,232.7	8,538.8	8,496.3	9,024.3	9,257.8
Currency in circulation	1,786.6	1,719.0	1,883.9	2,159.6	2,178.7	2,059.4	2,134.9	2,043.3	2,321.6	2,239.3	2,275.5	2,375.2	2,397.8
Total deposits	4,130.2	4,326.5	4,991.5	5,198.1	4,751.9	5,230.1	5,424.8	5,245.2	5,911.1	6,299.5	6,220.8	6,649.1	6,860.0
Demand deposits	2,342.1	2,616.5	2,825.8	3,266.1	2,776.7	3,133.1	3,308.6	3,182.4	3,482.5	3,737.9	3,671.9	3,941.8	4,082.7
Quasi money	1,788.2	1,710.0	2,165.7	1,932.0	1,975.2	2,097.1	2,116.2	2,062.7	2,428.7	2,561.6	2,548.9	2,707.3	2,777.3
Of which													
Resident deposits in foreign currencies	841.4	822.0	972.0	773.9	833.3	862.3	913.2	915.2	958.7	1,054.8	1,112.0	1,086.3	1,016.6
Short-term obligations	169.3	170.9	202.2	172.7	197.1	177.3	204.9	154.8	201.0	212.9	207.4	225.8	237.2
Memorandum items:	(Growth rate from end of previous year in percentage of end-of-year money stock, unless otherwise indicated)												
Net foreign assets	5.9	7.9	9.7	9.5	1.7	1.3	1.3	-3.7	2.1	0.3	1.3	4.1	4.7
Net domestic assets	12.2	-2.8	5.9	15.4	-2.2	-2.7	1.1	2.3	9.3	3.5	2.0	5.7	7.9
Net credit to government 2/	2.8	-7.5	4.8	10.5	-0.5	-0.6	3.2	5.0	9.1	2.3	-0.3	2.1	3.6
Credit to the economy 2/	9.2	7.8	2.8	6.1	-1.2	1.4	-0.8	-1.3	3.0	1.4	2.9	4.5	5.6
Change from previous year (in percent)	23.5	19.3	6.8	15.0	-3.2	3.8	-2.2	-3.5	7.8	3.9	7.9	12.3	15.4
Broad money (M3)	18.8	5.2	16.2	24.4	-0.4	-0.9	2.7	-0.9	11.9	3.7	3.2	9.6	12.5

Sources: Central Bank of Madagascar; and Fund staff estimates and projections.

1/ The increase in credit to government in the first quarter of 2003 reflects the expected assumption by the government of central bank credit to the state petroleum company under liquidation, SOLIMA, of FMG 350.4 billion.

2/ In 2003, growth of credit to government and the economy does not take into account the reclassification of the central bank claim on the state petroleum company under liquidation, SOLIMA, from credit to the economy to credit to the government, following the government takeover of SOLIMA debt to the central bank. This is assumed to take place in the first quarter of 2003, in an amount of FMG 350.4 billion.

Table 7. Madagascar: Summary Accounts of the Central Bank, 2000-03

(In billions of Malagasy francs; end of period)

	2000	2001			2002					2003			
	Dec.	Dec.			Mar.		Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.
	Act.	Prog.	Rev. Prog.	Act.	Prog.	Prov.	Prov.	Prel.	Prog.	Prog.	Prog.	Prog.	Prog.
Net foreign assets	1,170.5	1,872.2	1,616.9	1,787.7	1,892.9	1,746.2	1,693.6	1,275.7	1,658.1	1,571.9	1,595.4	1,851.5	1,981.8
Foreign assets	1,866.9	2,227.7	2,471.6	2,644.1	2,835.4	2,643.3	2,585.5	2,189.8	2,651.1	2,579.9	2,698.3	2,970.6	3,199.2
Foreign liabilities (short term)	-13.7	-18.9	-18.4	-12.2	-12.1	-15.9	-10.7	-18.1	-18.1	-18.4	-18.7	-19.0	-19.2
Poverty Reduction and Growth Facility	-682.7	-855.8	-836.3	-844.2	-930.4	-881.1	-881.1	-896.0	-974.9	-989.6	-1,084.2	-1,100.2	-1,198.2
Long-term foreign liabilities	-167.5	-165.4	-149.5	-149.0	-147.6	-155.5	-155.5	-161.5	-161.7	-164.2	-166.6	-169.1	-171.5
Net domestic assets	1,608.9	1,316.0	1,345.1	1,746.5	1,460.3	1,512.5	1,931.7	2,100.3	2,304.3	2,282.6	2,186.7	2,354.2	2,430.3
Claims on government (net)	1,162.7	628.8	930.1	1,207.8	919.4	1,078.6	1,377.0	1,567.4	1,870.2	2,228.9	2,160.6	2,356.4	2,466.6
Credit to government	2,023.0	1,662.4	1,763.7	2,096.5	1,811.2	2,103.3	2,155.3	2,180.1	2,242.6	2,601.3	2,533.0	2,728.8	2,839.0
Statutory advances	377.5	0.0	113.1	448.5	176.5	418.5	454.4	449.9	449.9	449.9	268.5	455.9	449.9
Consolidated loans [1]	1,099.6	1,099.6	1,099.6	1,099.6	1,099.6	1,099.6	1,099.6	1,099.6	1,099.6	1,450.0	1,450.0	1,450.0	1,450.0
Foreign currency loans [2]	533.5	553.8	542.0	540.1	535.0	571.1	571.1	550.0	550.9	559.2	567.5	575.9	584.2
Other	12.4	0.0	9.0	8.4	0.0	14.0	30.2	80.5	40.6	40.6	40.6	40.6	40.6
Government deposits	-860.3	-1,033.6	-833.6	-888.7	-891.7	-1,024.7	-778.3	-612.7	-372.4	-372.4	-372.4	-372.4	-372.4
Claims on public companies and customers	111.2	15.8	127.0	276.4	256.4	361.7	367.0	366.3	366.3	15.9	15.9	15.9	15.9
Net claims on banks	59.5	47.7	47.7	40.4	40.4	37.8	33.8	-9.1	-9.1	-9.1	-9.1	-9.1	-9.1
Claims on banks	59.5	63.4	47.7	40.4	40.4	37.8	33.8	30.9	30.9	30.9	30.9	30.9	30.9
Negative auctions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	-40.0	-40.0	-40.0	-40.0	-40.0	-40.0
Other items (net)	275.5	248.0	240.4	221.9	244.1	34.4	153.9	175.7	76.8	46.9	19.2	-9.0	-43.1
Currency valuation adjustment	85.5	47.1	105.5	56.0	41.1	-47.6	-29.1	4.8	-94.0	-124.0	-151.6	-179.9	-214.0
Net capital	-116.3	-103.9	-118.1	-116.3	-116.3	-115.8	-115.8	-116.2	-116.2	-116.2	-116.2	-116.2	-116.2
Others	306.3	119.2	253.0	282.3	319.3	197.8	298.8	287.1	287.1	287.1	287.1	287.1	287.1
Reserve money	2,610.0	2,612.9	2,812.2	3,384.9	3,205.2	3,102.7	3,469.4	3,214.1	3,800.1	3,689.9	3,615.0	4,036.1	4,240.2
Currency outside banks	1,786.6	1,719.0	1,883.9	2,159.6	2,178.7	2,059.4	2,134.9	2,043.3	2,321.6	2,239.3	2,275.5	2,375.2	2,397.8
Currency in banks	78.4	69.0	97.4	84.9	92.2	197.1	258.3	182.2	116.1	123.9	122.0	130.8	135.0
Bank deposits	745.0	803.6	830.9	1,140.4	934.3	846.3	1,076.2	988.5	1,362.4	1,326.8	1,217.5	1,530.1	1,707.4
Deposits of other banking institutions	1.7	4.8	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Resident deposits in foreign currency	0.1	0.2	0.2	0.2	0.2	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3

Sources: Central Bank of Madagascar; and Fund staff estimates and projections.

[1] The increase in credit to government in the first quarter of 2003 reflects the expected assumption by the government of central bank credit to the state petroleum company under liquidation, SOLIMA, of FMG 350.4 billion.

[2] The increase in 2003 reflects valuation adjustment.

Table 8. Madagascar: Summary Accounts of Commercial Banks, 2000-03

(In billions of Malagasy francs unless otherwise indicated; end of period)

	2000	2001			2002					2003			
	Dec.	Dec.			Mar.		Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.
	Act.	Prog.	Rev. Prog.	Prov.	Prog.	Prov.	Prov.	Prel.	Prog.	Prog.	Prog.	Prog.	Prog.
Net bank liquidity	1,538.0	1,452.7	1,797.0	1,853.1	1,796.1	1,849.4	2,187.5	2,134.7	2,490.9	2,569.2	2,520.8	2,812.6	2,915.4
Net foreign assets	835.9	672.2	965.6	783.5	859.2	923.5	976.3	1,019.7	1,068.2	1,175.4	1,239.1	1,210.5	1,132.7
Of which: nonresident nonbank deposits	107.9	136.7	196.4	101.1	174.8	119.2	126.0	131.6	137.9	151.7	160.0	156.3	146.2
Long-term foreign liabilities	-61.7	-49.4	-49.3	-115.2	-49.3	-79.7	-89.5	-64.8	-64.9	-65.9	-66.9	-67.9	-68.8
Reserves	823.4	893.4	928.3	1,225.3	1,026.5	1,043.3	1,334.5	1,170.8	1,478.5	1,450.6	1,339.5	1,660.9	1,842.4
Currencies in banks	78.4	69.0	97.4	84.9	92.2	197.1	258.3	182.2	116.1	123.9	122.0	130.8	135.0
Deposits at central bank	745.0	824.4	830.9	1,140.4	934.3	846.3	1,076.2	988.5	1,362.4	1,326.8	1,217.5	1,530.1	1,707.4
Net recourse to central bank	59.5	63.4	47.7	40.4	40.4	37.8	33.8	-9.1	-9.1	-9.1	-9.1	-9.1	-9.1
Net domestic assets	2,296.6	2,675.7	2,875.5	2,914.2	2,632.8	2,938.5	2,803.3	2,676.4	2,986.2	3,273.9	3,233.8	3,360.7	3,459.1
Claims on government (net)	400.6	550.7	894.4	840.0	873.0	913.1	902.6	847.4	840.0	1,002.7	840.0	840.0	840.0
Credit to government	606.5	691.7	1,130.4	1,182.4	1,181.1	1,255.6	1,267.0	1,243.6	1,223.8	1,386.5	1,223.8	1,223.8	1,223.8
Government deposits	-205.9	-140.9	-236.0	-342.4	-308.2	-342.4	-364.4	-396.2	-383.8	-383.8	-383.8	-383.8	-383.8
Of which: deposits of administrative agencies	-197.2	-136.3	-228.3	-332.8	-298.1	-333.3	-354.7	-386.7	-420.4	-442.1	-451.5	-460.9	-470.3
Claims on private sector	2,303.3	2,604.6	2,451.4	2,500.8	2,247.2	2,519.1	2,350.6	2,311.8	2,629.0	2,743.8	2,866.4	2,993.3	3,091.7
Of which: in foreign currency	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
In millions of SDRs	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net capital	-517.9	-632.0	-613.9	-620.7	-631.9	-636.4	-659.2	-681.9	-681.9	-671.7	-671.7	-671.7	-671.7
Other items (net)	110.6	152.4	143.6	194.1	144.5	142.7	209.4	199.1	199.1	199.1	199.1	199.1	199.1
Currency valuation adjustment	-0.9	-4.1	-0.8	-0.5	0.1	-0.7	-0.9	-0.4	-0.4	-0.4	-0.4	-0.4	-0.4
Other	111.5	152.4	144.4	194.6	144.4	143.3	210.3	199.5	199.5	199.5	199.5	199.5	199.5
Deposits	3,665.3	3,957.5	4,470.3	4,594.5	4,231.8	4,610.6	4,785.9	4,656.3	5,276.0	5,630.2	5,547.3	5,947.4	6,137.3
Demand deposits	2,228.9	2,575.9	2,689.1	3,074.1	2,638.4	2,929.7	3,113.5	2,987.3	3,287.3	3,532.6	3,462.3	3,727.8	3,864.4
Time deposits	595.2	559.8	809.3	746.7	760.3	818.9	759.5	754.2	1,030.3	1,043.0	973.2	1,133.6	1,256.6
Foreign currency	841.3	821.8	971.9	773.7	833.1	862.0	912.9	914.9	958.4	1,054.5	1,111.7	1,086.0	1,016.3
In millions of SDRs	98.5	98.7	117.8	92.9	101.0	98.6	97.8	102.1	106.8	115.8	120.3	115.8	106.8
Short-term bonds	169.3	170.9	202.2	172.7	197.1	177.3	204.9	154.8	201.0	212.9	207.4	225.8	237.2

Sources: Central Bank of Madagascar; and Fund staff estimates and projections.

Table 9. Madagascar: Balance of Payments, 1998-2006
(In millions of SDRs, unless otherwise indicated)

	1998	1999	2000		2001		2002		2003	2004	2005	2006
			Rev. Prog.	Act.	Prog.	Act.	Proj.	Rev. Proj.	Projections			
Current account	-207.3	-153.7	-210.9	-165.4	-200.6	-46.4	-299.4	-155.0	-211.1	-209.9	-219.0	-232.5
Goods and services	-216.2	-217.2	-300.7	-214.8	-262.7	-114.3	-325.8	-202.4	-292.5	-291.8	-310.1	-333.8
Trade balance	-112.9	-122.3	-201.4	-78.6	-90.6	11.6	-79.2	-91.3	-122.0	-116.5	-125.5	-139.4
Exports	382.6	425.9	462.0	628.5	718.4	757.9	771.8	406.0	535.0	591.0	644.6	702.3
Imports	-495.5	-548.2	-663.5	-707.1	-809.0	-746.3	-851.0	-497.3	-657.0	-707.5	-770.1	-841.7
Net services	-103.3	-94.8	-99.3	-136.2	-172.1	-125.9	-246.6	-111.1	-170.5	-175.3	-184.6	-194.4
Services, receipts	208.1	238.5	270.3	270.9	283.5	276.3	264.0	181.1	240.7	262.4	286.5	313.3
Transportation	43.5	40.5	46.7	39.8	47.1	48.2	49.6	25.8	34.0	36.3	38.7	41.2
Travel	65.5	72.8	85.2	91.9	92.1	90.2	87.3	39.8	70.1	81.3	94.3	109.4
Business and personal services	79.8	98.7	109.9	100.6	101.5	77.3	80.0	64.8	76.6	81.2	86.0	91.2
Other Government services	19.3	26.5	28.5	38.7	42.7	60.6	47.0	50.8	60.0	63.6	67.5	71.5
Services, payments	-311.4	-333.3	-369.6	-407.1	-455.6	-402.2	-510.6	-292.3	-411.2	-437.7	-471.0	-507.6
Transportation	-101.7	-109.1	-146.6	-161.1	-184.7	-182.1	-215.5	-131.7	-177.2	-181.4	-195.6	-211.6
Travel	-84.8	-81.3	-82.0	-87.9	-107.6	-102.1	-112.7	-72.0	-102.0	-108.1	-114.6	-121.4
Business and personal services	-46.7	-55.3	-45.6	-62.1	-60.3	-50.0	-63.2	-41.9	-51.7	-54.8	-58.1	-61.6
Other Government services	-78.2	-87.6	-95.4	-96.0	-103.1	-68.0	-119.2	-46.6	-80.4	-93.4	-102.7	-113.0
Income	-54.2	-31.1	-32.9	-53.3	-68.5	-46.7	-86.0	-58.5	-53.9	-42.6	-43.0	-43.3
Receipts	18.0	15.1	17.1	16.6	15.0	18.7	15.3	15.5	19.5	20.2	20.9	21.6
Investment income	9.5	6.6	8.6	8.4	6.5	10.2	6.8	7.2	11.0	11.7	12.4	13.1
Other	8.5	8.5	8.5	8.2	8.5	8.5	8.5	8.3	8.5	8.5	8.5	8.5
Payments	-72.2	-46.2	-50.1	-69.9	-83.5	-65.4	-101.3	-74.0	-73.3	-62.8	-63.9	-64.9
Dividends	-5.0	-6.4		-20.0	-30.0	-30.0	-46.3	-27.7	-32.3	-34.3	-36.3	-38.5
Interest	-67.2	-39.8	-43.1	-40.9	-44.5	-44.4	-50.0	-47.3	-46.0	-33.5	-32.5	-31.4
Of which: government interest [1]	-63.2	-38.0	-40.1	-39.6	-41.6	-41.4	-46.6	-43.9	-43.2	-30.7	-29.9	-29.0
Current transfers	63.0	94.6	122.7	102.6	130.6	114.6	112.4	105.9	135.2	124.5	134.1	144.5
Government	12.6	25.8	44.7	25.5	58.4	24.9	38.0	44.9	62.6	39.5	41.3	43.2
Budget aid	8.1	20.8	36.1	16.5	49.4	36.7	28.8	51.3	53.1	30.0	31.8	33.7
Of which: HIPC relief [2]	0.0	0.0	0.0	0.0	18.8	18.8	20.2	20.2	22.2	0.0	0.0	0.0
Other (net) [3]	4.5	5.0	8.7	9.0	9.0	-11.8	9.2	-6.4	9.5	9.5	9.5	9.5
Private	50.4	68.8	78.0	77.1	72.2	89.7	74.4	61.0	72.6	85.0	92.8	101.3
Capital and financial account	80.7	143.7	198.1	83.2	208.0	67.6	267.3	67.5	150.7	223.8	242.7	258.3
Capital transfers	73.5	94.2	101.0	87.0	106.3	88.6	144.9	40.4	63.5	87.5	92.7	98.3
Government	73.5	94.2	101.0	87.0	106.3	88.6	144.9	40.4	63.5	87.5	92.7	98.3
Project grants	73.5	94.2	101.0	87.0	106.3	88.6	144.9	40.4	63.5	87.5	92.7	98.3
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Private sector	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial account	24.4	41.8	90.6	35.0	147.6	91.1	122.4	27.1	87.2	136.3	150.0	160.0
Direct investment	11.9	42.7	54.4	52.9	85.0	73.1	60.3	5.0	33.4	52.0	60.6	70.6
Of which: privatization receipts	0.7	15.4	20.6	5.3	21.0	10.9	23.1	3.0	16.0	15.0	0.0	0.0
Portfolio investments	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	12.5	-0.9	36.2	-17.9	62.6	18.0	62.1	22.1	53.8	84.4	89.4	89.4
Government	0.5	-2.1	36.2	7.1	83.0	21.5	65.1	54.6	62.7	91.2	96.4	96.4
Drawings	90.2	75.0	114.7	86.9	158.6	90.2	145.6	126.7	133.7	137.0	143.3	149.9
project drawings	64.0	56.5	72.3	46.2	96.7	60.4	106.6	47.4	105.0	105.0	111.3	117.9
budgetary support	19.3	11.6	39.4	39.3	58.9	26.8	34.0	79.3	22.7	25.0	25.0	25.0
of which: SAC II	0.0	0.0	25.8	25.8	23.3	0.0	34.0	56.5	0.0	20.0	20.0	20.0
Nongovernment	6.9	6.9	3.0	1.4	3.0	3.0	5.0	0.0	6.0	7.0	7.0	7.0
Amortization [1]	-89.7	-77.1	-78.5	-79.8	-75.5	-68.7	-80.5	-72.1	-71.0	-45.8	-46.8	-53.5
Private sector	-5.3	-1.3	0.0	0.0	0.0	-7.3	7.0	-7.5	-8.9	-6.8	-7.0	-7.0
Drawings	0.0	0.0	...	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Amortization	-5.3	-1.3	...	0.0	0.0	-7.3	0.0	-7.5	-8.9	-6.8	-7.0	-7.0
Banks (net)	17.3	2.4	0.0	-25.0	-20.4	3.8	-10.0	-25.0	0.0	0.0	0.0	0.0
Other (including errors and omissions) [4]	-17.2	7.8	6.5	-38.9	-45.9	-112.2	0.0	0.0	0.0	0.0	0.0	0.0
Of which: indemnification	-2.5	-4.5	-9.7	-4.9	-9.0	-3.3	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-126.6	-9.9	-12.9	-82.3	7.4	21.1	-32.2	-87.5	-60.4	13.9	23.7	25.8

Table 9. Madagascar: Balance of Payments, 1998-2006 (concluded)
(In millions of SDRs, unless otherwise indicated)

	1998	1999	2000 Rev. Prog.	2000 Act.	2001 Prog.	2001 Act.	2002 Proj.	2002 Rev. Proj.	2003	2004	2005	2006
									Projections			
Financing	126.6	9.9	12.8	82.3	-7.4	-21.1	32.2	87.5	60.4	-13.9	-23.7	-25.8
Net foreign assets (increase -)	76.6	-34.0	-28.9	28.4	-60.4	-76.9	-27.3	30.0	-23.5	-13.9	-23.7	-25.8
Use of Fund credit (net)	-10.3	9.7	34.2	34.2	21.4	21.4	20.0	8.6	17.3	17.3	-5.4	-5.4
Purchase	0.0	13.6	38.0	38.0	22.7	22.7	22.7	11.4	22.7	22.7	0.0	0.0
Repurchases	-10.3	-3.8	-3.8	-3.8	-1.3	-1.3	-2.7	-2.7	-5.4	-5.4	-5.4	-5.4
Other assets (net increase -)	86.9	-43.7	-63.1	-5.7	-81.8	-98.3	-47.3	21.4	-40.8	-31.2	-18.3	-20.4
Net change in arrears (excluding central bank) [5]	12.0	3.1	-4.9	-5.7	-8.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Arrears accumulation	18.1	3.1	...	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repayment of arrears	-6.1	0.0	...	-5.7	0.0	-8.1	0.0	0.0	0.0	0.0	0.0	0.0
Rescheduling of arrears	0.0	0.0	...	0.0	-8.1	8.1	0.0	0.0	0.0	0.0	0.0	0.0
Cancellation of arrears												
Debt relief and cancellation [5 6]	38.0	40.8	46.6	59.6	61.1	55.8	59.5	57.5	50.1	0.0	0.0	0.0
Current maturities	38.0	40.8	46.6	59.6	53.0	55.8	59.5	57.5	50.1	0.0	0.0	0.0
Arrears	0.0	0.0	0.0	0.0	8.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Residual financing gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	33.8	0.0	0.0	0.0
Of which: Paris Club	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
supplementary relief	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:												
Grants/ GDP (in percent)	3.1	4.4	5.0	3.8	4.6	3.1	4.6	2.5	3.4	3.2	3.2	3.1
Loans/ GDP (in percent)	0.0	-0.1	1.2	0.2	2.3	0.6	1.6	1.6	1.7	2.3	2.3	2.1
Direct investment / GDP (in percent)	0.4	1.6	1.8	1.8	2.4	2.0	1.5	0.1	0.9	1.3	1.4	1.5
External current account / GDP (in percent)												
Excluding net official transfers	-8.0	-6.6	-8.7	-6.5	-7.2	-2.0	-8.5	-5.8	-7.4	-6.4	-6.1	-6.0
Including net official transfers	-7.5	-5.6	-7.2	-5.6	-5.6	-1.3	-7.5	-4.5	-5.7	-5.4	-5.2	-5.1
Debt service-to-exports ratio [7] (before debt relief)	27.5	17.8	13.6	13.4	12.0	11.6	12.6	21.8	16.3	15.5	14.0	14.1
Debt service-to-exports ratio [7] (after debt relief)	21.0	11.6	10.3	6.8	4.8	4.4	4.9	8.6	6.9	8.5	7.8	7.7
Debt service to revenue ratio [8] (before relief)	55.3	38.0	30.3	35.2	26.0	33.3	21.7	51.6	32.3	31.3	28.0	27.8
Debt service-to-revenue ratio [8] (after relief)	42.3	24.9	...	17.8	...	12.7	33.4	20.3	13.7	17.2	15.6	15.2
Annual percentage changes												
Export volume	9.5	17.2	6.5	26.3	9.6	9.5	9.8	-46.9	40.4	7.8	6.0	6.8
Import volume	7.3	8.7	5.9	19.3	18.0	6.6	7.9	-32.9	32.6	8.7	6.7	6.6
Real GDP	3.9	4.7	5.9	6.0	6.7	6.0	4.8	-11.8	7.8	6.0	6.0	6.0
Gross official reserves	121.8	165.5	146.3	218.7	298.9	317.5	346.2	296.1	336.9	368.1	386.4	406.8
(weeks of goods and nonfactor services imports)	7.8	9.8	7.4	10.2	12.3	14.4	13.2	19.5	16.4	16.7	16.2	15.7
Exchange rates												
Malagasy francs/SDR (period average)	7,381.7	8,585.8	...	8,934.0	...	8,385.8	...		...	...	...	...
Malagasy francs/U.S. dollar (period average)	5,441.4	6,283.8	...	6,773.3	...	6,587.2	...	...	...	...	...	...

Sources: Central Bank of Madagascar; and Fund staff estimates and projections.

[1] For 2004, interest and amortization are calculated after the stock-of-debt reduction expected to take place at end-2003, assuming attainment of the completion point under the enhanced HIPC Initiative at end-2003.

[2] Interim relief is being provided by the African Development Bank Group (AfDB), IDA, and the IMF for 2001-03. The distribution of interim relief among these years differs from the original program due to AfDB's choice of a different delivery option than assumed at the time of the decision point.

[3] Other official grants less payments due to scholarships and contributions to international organizations.

[4] Includes commercial credits received or granted.

[5] Bilateral agreements on debt with non-Paris Club creditors, most of which is in arrears, were initially assumed to be finalized in 2001; however, such reschedulings are materializing at a slower pace than envisaged. For 2001, arrears were rescheduled with the Saudi Fund and a commercial creditor, Itochu Bank (Hong-Kong SAR).

[6] Assuming a flow rescheduling on Cologne terms in 2001, of which a part is attributable to HIPC Initiative relief.

[7] In percent of exports of goods and nonfactor services.

[8] In percent of government revenue.

Table 10. Madagascar: External Debt Sustainability Indicators, 2000-19

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Average 2000-09	Average 2010-19
	(In percent)																					
After traditional debt relief																						
Current estimates																						
NPV of debt-to-exports ratio	220.4	192.7	209.5	229.8	253.9	225.5	212.8	201.5	190.1	179.4	169.8	161.3	153.2	145.7	138.7	132.0	125.8	119.9	114.3	109.0 #	208.7	132.2
NPV of debt-to-revenue ratio	469.7	476.5	708.9	459.8	428.6	391.7	358.2	327.3	298.6	273.0	250.5	231.0	213.4	201.4	190.2	179.8	170.0	160.9	152.3	144.3 #	382.6	180.6
NPV of debt-to-GDP ratio	54.9	47.6	50.8	48.6	47.4	45.3	43.2	41.1	39.0	37.0	35.2	33.6	32.1	30.7	29.4	28.2	27.0	25.8	24.8	23.8 #	44.4	28.2
Debt service-to-export ratio	12.9	10.6	11.8	12.2	13.6	11.5	11.5	10.8	10.3	10.0	9.2	8.3	7.6	6.8	6.0	5.5	5.1	4.8	4.6	4.3 #	11.4	5.8
Debt service-to-revenue ratio	27.5	26.2	39.9	24.4	22.9	20.0	19.4	17.5	16.2	15.3	13.6	11.9	10.6	9.4	8.2	7.5	6.9	6.5	6.2	5.7 #	20.8	8.0
Decision point estimates																						
NPV of debt-to-exports ratio	239.7	229.0	220.4	210.0	194.4	180.7	168.5	159.9	151.8	143.9	136.8	131.2	125.9	120.9	116.1	111.2	106.3	101.6	97.0	92.5 #	182.0	111.0
NPV of debt-to-revenue ratio	435.6	409.4	375.4	343.1	313.3	286.3	262.1	240.3	220.7	202.7	186.9	173.5	161.1	149.6	138.7	128.6	119.1	110.4	102.2	94.6 #	285.0	127.8
NPV of debt-to-GDP ratio	55.0	52.2	48.5	45.3	42.3	39.5	37.0	34.6	32.4	30.4	28.6	27.1	25.6	24.2	22.9	21.6	20.4	19.2	18.1	17.0 #	39.6	21.6
Debt service-to-export ratio	12.7	12.0	11.0	10.7	10.4	9.8	10.2	9.9	9.6	9.4	8.9	7.9	7.9	7.9	7.9	7.9	7.8	7.7	7.5	7.4 #	10.4	7.8
Debt service-to-revenue ratio	23.1	21.4	18.8	17.4	16.7	15.5	15.9	14.9	14.0	13.3	12.2	10.4	10.1	9.7	9.4	9.1	8.8	8.3	7.9	7.5 #	16.2	9.0
After enhanced HIPC assistance																						
Current estimates [1]																						
NPV of debt-to-exports ratio	259.2	182.6	128.6	145.0	164.1	148.8	143.5	138.8	133.4	128.4	124.0	120.3	116.8	113.4	110.3	107.4	104.4	101.7	99.0	96.4 #	153.6	107.2
NPV of debt-to-revenue ratio	552.4	451.5	435.0	290.1	277.0	258.5	241.5	225.4	209.5	195.4	182.9	172.4	162.6	156.8	151.3	146.2	141.2	136.5	132.0	127.6 #	281.7	146.4
NPV of debt-to-GDP ratio	64.6	45.1	31.2	30.6	30.6	29.9	29.1	28.3	27.4	26.5	25.7	25.1	24.5	23.9	23.4	22.9	22.4	21.9	21.5	21.0 #	32.7	22.9
Debt service-to-export ratio	6.7	3.9	4.6	5.2	7.4	6.4	6.3	5.9	5.6	5.4	4.8	3.7	3.3	2.9	2.5	2.3	2.1	1.9	1.8	1.6 #	5.7	2.5
Debt service-to-revenue ratio	14.3	9.8	15.7	10.4	12.6	11.1	10.6	9.6	8.8	8.2	7.0	5.3	4.6	4.0	3.4	3.1	2.8	2.6	2.4	2.2 #	10.5	3.4
Decision point estimates [2]																						
NPV of debt-to-exports ratio	281.6	217.2	136.7	133.1	125.1	118.3	112.0	108.1	104.4	100.8	97.7	95.8	94.0	92.3	90.5	88.6	86.5	84.5	82.4	80.3 #	133.3	88.1
NPV of debt-to-revenue ratio	511.6	388.4	232.8	217.5	201.6	187.3	174.3	162.5	151.8	142.1	133.5	126.8	120.3	114.1	108.1	102.5	97.0	91.8	86.9	82.1 #	208.7	101.5
NPV of debt-to-GDP ratio	64.5	49.5	30.1	28.7	27.2	25.9	24.6	23.4	22.3	21.3	20.4	19.8	19.1	18.5	17.8	17.2	16.6	16.0	15.4	14.8 #	29.0	17.1
Debt service-to-export ratio	11.7	6.6	5.4	6.0	6.2	5.9	6.5	6.4	6.3	6.2	5.8	4.9	5.1	5.2	5.3	5.3	5.4	5.4	5.3	5.3 #	6.6	5.3
Debt service-to-revenue ratio	21.2	11.8	9.2	9.7	10.0	9.3	10.1	9.7	9.2	8.8	8.0	6.5	6.6	6.4	6.3	6.1	6.1	5.8	5.6	5.4 #	10.3	6.1
	(In millions of U.S. dollars, unless otherwise indicated)																					
Memorandum items:																						
GDP																						
Current estimates	3,874	4,605	4,483	4,893	5,218	5,651	6,129	6,653	7,219	7,832	8,498	9,221	10,004	10,855	11,777	12,778	13,865	15,043	16,322	17,709	5,656	12,607
Decision point estimates	3,906	4,283	4,773	5,291	5,806	6,376	6,960	7,598	8,295	9,055	9,885	10,791	11,780	12,860	14,039	15,326	16,731	18,264	19,938	21,766	6,234	15,138
Exports (three-year moving average)																						
Current estimates	965	1,137	1,087	1,034	975	1,135	1,244	1,358	1,481	1,616	1,763	1,924	2,099	2,290	2,498	2,725	2,973	3,244	3,539	3,861	1,203	2,692
Decision point estimates	896	976	1,051	1,141	1,263	1,394	1,527	1,645	1,773	1,914	2,066	2,228	2,398	2,577	2,769	2,978	3,208	3,454	3,720	4,008	1,358	2,941
Exports (current year)																						
Current estimates	1,186	1,317	759	1,027	1,138	1,241	1,354	1,478	1,612	1,759	1,919	2,093	2,284	2,492	2,718	2,966	3,236	3,530	3,851	4,202	1,287	2,929
Decision point estimates	972	1,046	1,135	1,242	1,412	1,528	1,641	1,767	1,910	2,065	2,224	2,395	2,576	2,759	2,972	3,203	3,450	3,710	4,000	4,313	1,472	3,160
Revenue excluding grants																						
Current estimates	453	460	321	517	577	654	739	836	943	1,062	1,195	1,343	1,507	1,657	1,821	2,002	2,199	2,416	2,654	2,916	656	1,971
Decision point estimates	493	546	617	699	784	880	982	1,094	1,220	1,358	1,513	1,684	1,873	2,084	2,317	2,575	2,861	3,178	3,530	3,918	867	2,553
NPV of debt (after traditional debt relief)																						
Current estimates	2,127	2,191	2,278	2,377	2,474	2,560	2,648	2,736	2,816	2,900	2,994	3,102	3,216	3,337	3,464	3,599	3,739	3,888	4,044	4,208	2,511	3,559
Decision point estimates	2,147	2,235	2,316	2,397	2,456	2,519	2,573	2,630	2,691	2,754	2,827	2,922	3,018	3,116	3,214	3,312	3,409	3,508	3,607	3,706	2,472	3,264
Debt service (after traditional debt relief)																						
Current estimates	125	120	128	126	132	131	143	146	153	162	162	160	160	155	149	149	151	156	163	167	137	157
Decision point estimates	114	117	116	122	131	137	156	163	171	180	184	176	190	203	219	234	250	264	280	295	141	229
NPV of debt (after enhanced HIPC assistance)																						
Current estimates	2,502	2,076	1,398	1,499	1,599	1,690	1,786	1,884	1,976	2,075	2,186	2,315	2,451	2,597	2,755	2,926	3,104	3,298	3,504	3,721	1,848	2,886
Decision point estimates	2,521	2,120	1,436	1,519	1,581	1,649	1,711	1,778	1,851	1,930	2,020	2,135	2,253	2,377	2,505	2,639	2,775	2,918	3,067	3,219	1,810	2,591
Debt service (after enhanced HIPC assistance)																						
Current estimates [3]	65	45	50	54	73	73	78	81	83	87	84	71	70	66	63	61	62	62	64	63	69	67
Decision point estimates	105	64	56	68	79	82	99	106	112	120	120	110	123	134	147	158	175	185	197	213	89	156

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

[1] Assumes that the completion point is reached in December 2003; HIPC Initiative assistance is assumed to be comitted and delivered unconditionally from then.

[2] The decision point document assumes that the completion point is reached in December 2002.

[3] Current numbers for 2000-01 are on a cash basis, and so do not need to be consistent with decision point estimates.

Table 11. Madagascar: Tracking Delivery of HIPC Assistance

	Contact with Creditor	Agreement to Provide HIPC		Agreement to Provide Interim Assistance		Delivery of Interim Assistance		Delivery of Completion Pt. Assist.	
	Date	Status	Date	Status	Date	Status	Date	Date	Comments
Multilateral creditors									
IMF	18-Dec-00	yes	18-Dec-00	yes		yes			
IDA	22-Dec-00	yes	22-Dec-00	yes		yes			
AfDB/AfDF	19-Feb-01	yes	24-Apr-01	yes		yes			
IFAD	19-Feb-01	yes		limited		no			
EU/EIB	19-Feb-01	yes		yes		no			Letter to EIB.
OPEC	19-Feb-01	yes	26-Feb-02	limited		yes			Agreement.
BADEA	19-Feb-01	limited		limited		no			
Paris Club creditors [1,2]									
Austria		yes	10-Oct-01	yes		yes			
Belgium		yes	7-Mar-01	yes		yes			
Canada	21-Dec-00	yes	7-Mar-01	yes	25-Sep-02	yes			Letter on December 21, 2000 providing moratorium; agreement on Sep. 25, 2002.
France		yes	7-Mar-01	yes		yes			
Germany		yes	2-Jul-02	yes	2-Jul-02	yes			Agreement on July 02, 2002: stock and flow.
Israel		yes	7-Mar-01	yes		yes			
Italy		yes	22-May-01	yes	22-May-01	yes			Letter # 1712 announcing decision to cancel 100 percent of debt.
Japan		yes	7-Mar-01	yes		yes			
Russia		yes	7-Mar-01	yes		yes	6-Dec-01		Letter on post-cutoff-date debt on December 06, 2001: flow and stock.
Spain		yes	20-Sep-01	yes		yes			Agreement.
Switzerland		yes		yes	22-May-01	yes	18-Oct-01		Agreement: cancellation of 100 percent of restructured debt under PC 9.
Sweden		yes	7-Mar-01	yes		yes			
United Kingdom		yes	7-Mar-01	yes		yes			Ambassador's announcement on July 29, 2002 on moratorium.
USA		yes	7-Mar-01	yes		yes			
Non-Paris Club bilateral creditors									
Algeria	5-Nov-01	no		no		no			
Angola	8-Nov-01	no		no		no			
China	5-Nov-01	no		no		yes	12-Nov-01		Agreement.
Iraq	5-Nov-01	no		no		no			
Kuwait		no		no		yes	27-Sep-99		Agreement.
Libya	5-Nov-01	no		no		no			
United Arab Emirates	5-Nov-01	no		no		no			
Saudi Arabia		no		no		yes	24-Jan-01		Agreement.
Commercial creditors									
Creditors include:									
AGIP									
ENI International Lt Bank									
Hong Kong CITOH Bank				yes	27-Apr-01	yes			Agreement.
London Club debt									

Sources: Malagasy authorities; and IMF staff.

[1] Paris Club agreed minutes on restructuring from December 2000 to HIPC floating completion point.

[2] Letter sent to Malagasy authorities on September 25, 2002 notifying the missed implementation of the second phase of the Paris Club agreed minutes pending the second review of the PRGF arrangement with the IMF.

Table 12. Madagascar: Indicators of Fund Credit, 1997-2004
(in millions of SDRs, unless otherwise indicated)

	1997	1998	1999	2000	2001	2002 Proj.	2003 Proj.	2004 Proj.
Fund credit outstanding (end of period)	51.5	41.2	45.8	80.0	101.4	108.7	124.5	140.2
In millions of U.S. dollars	70.8	55.9	62.6	105.5	129.1	140.5	164.8	186.9
In millions of Malagasy francs	360.6	304.2	393.5	714.4	850.1	966.5	1,162.0	1,375.4
In percent of quota	56.9	45.6	37.5	65.4	83.0	88.9	101.9	114.7
Purchases from the Fund	13.6	0.0	13.6	38.0	22.7	11.4	22.7	22.7
Debt service to the Fund	13.9	11.3	4.8	4.9	2.5	4.1	6.9	7.0
In millions of U.S. dollars	19.1	15.4	6.6	6.5	3.2	5.3	9.1	9.4
In millions of Malagasy francs	97.2	83.6	41.5	43.9	21.2	36.2	64.2	68.9
Principal	12.9	10.3	3.8	3.8	1.3	2.7	5.4	5.4
Charges / interest	1.0	1.1	1.0	1.1	1.2	1.4	1.5	1.6
Debt service in percent of:								
Exports of goods and nonfactor services	2.5	1.9	0.7	0.5	0.2	0.7	0.9	0.8
Total debt service due before debt relief	8.8	7.0	4.1	4.1	2.1	3.2	5.5	5.3
Government revenue	5.6	3.9	1.6	1.4	0.7	1.6	1.8	1.7
GDP	0.5	0.4	0.2	0.2	0.1	0.1	0.2	0.2
Quota	15.4	12.5	4.0	4.0	2.1	3.3	5.6	5.7

Source: IMF staff.

Table 13. Madagascar: Supply and Use of Resources at Current Prices, 1997-2003 [1]
(In billions of Malagasy francs)

	1997	1998	1999	2000	2001	2002	2003
Gross domestic product at market prices	18,051	20,343	23,379	26,242	30,334	30,842	34,506
Net imports of goods and nonfactor services	1,461	1,578	1,809	1,919	959	1,800	2,730
Exports of goods and nonfactor services	3,947	4,378	5,715	8,036	8,672	5,223	7,241
of which: Exports of goods	2,585	2,842	3,667	5,615	6,355	3,611	4,994
Imports of goods and nonfactor services	5,408	5,956	7,524	9,954	9,631	7,023	9,972
of which: Imports of goods	3,477	3,658	4,662	6,317	6,258	4,423	6,133
Total available resources	19,512	21,921	25,188	28,161	31,292	32,642	37,236
Consumption	17,199	18,914	21,704	24,213	26,589	29,232	31,984
Government	1,960	2,089	2,175	2,403	3,082	3,251	3,548
Nongovernment	15,239	16,825	19,529	21,810	23,508	25,981	28,436
Investment	2,313	3,007	3,485	3,948	4,703	3,411	5,252
Government	1,177	1,612	1,616	1,766	2,181	1,149	2,496
Nongovernment	1,136	1,395	1,869	2,182	2,522	2,262	2,757
Gross domestic savings	852	1,429	1,675	2,029	3,744	1,610	2,522
Government	-213	76	492	665	-53	-1,000	69
Nongovernment	1,066	1,353	1,183	1,364	3,797	2,611	2,453
Current account							
Excluding grants	-1,405	-1,608	-1,483	-1,698	-598	-1,778	-2,555
Including grants	-1,000	-1,515	-1,261	-1,471	-389	-1,379	-1,971
Gross national savings	1,313	1,492	2,223	2,478	4,314	2,032	3,282
Government	192	169	714	893	156	-601	654
Nongovernment	1,121	1,322	1,509	1,585	4,157	2,633	2,628
Memorandum items:							
Private transfers	521	372	591	689	752	543	678
Net factor income	-466	-402	-264	-469	-392	-521	-503
Current official grants	406	93	222	228	209	399	585
Total	461	63	548	448	569	421	760
				(In percent of GDP)			
Net imports of goods and nonfactor services	8.1	7.8	7.7	7.3	3.2	5.8	7.9
Exports of goods and nonfactor services	21.9	21.5	24.4	30.6	28.6	16.9	21.0
Imports of goods and nonfactor services	30.0	29.3	32.2	37.9	31.8	22.8	28.9
Total available resources	108.1	107.8	107.7	107.3	103.2	105.8	107.9
Consumption	95.3	93.0	92.8	92.3	87.7	94.8	92.7
Government	10.9	10.3	9.3	9.2	10.2	10.5	10.3
Nongovernment	84.4	82.7	83.5	83.1	77.5	84.2	82.4
Investment	12.8	14.8	14.9	15.0	15.5	11.1	15.2
Government	6.5	7.9	6.9	6.7	7.2	3.7	7.2
Nongovernment	6.3	6.9	8.0	8.3	8.3	7.3	8.0
Domestic savings	4.7	7.0	7.2	7.7	12.3	5.2	7.3
Government	-1.2	0.4	2.1	2.5	-0.2	-3.2	0.2
Nongovernment	5.9	6.6	5.1	5.2	12.5	8.5	7.1
Current account							
Excluding grants	-7.8	-7.9	-6.3	-6.5	-2.0	-5.8	-7.4
Including grants	-5.5	-7.4	-5.4	-5.6	-1.3	-4.5	-5.7
Gross national savings	7.3	7.3	9.5	9.4	14.2	6.6	9.5
Government	1.1	0.8	3.1	3.4	0.5	-1.9	1.9
Nongovernment	6.2	6.5	6.5	6.0	13.7	8.5	7.6
Memorandum items:							
Private transfers	2.9	1.8	2.5	2.6	2.5	1.8	2.0
Net factor income	-2.6	-2.0	-1.1	-1.8	-1.3	-1.7	-1.5
Current official grants	2.2	0.5	0.9	0.9	0.7	1.3	1.7

Sources: Ministry of Economy, Finance, and Budget; and Fund staff estimates.

Table 14: Regional Poverty in Madagascar by Area of Residence: 1993-2001 [1]

	Headcount				Depth		
	1993	1997	1999	2001	1993	1997	1999
Urban Poverty							
Total	50.1	63.2	52.1	50.0	17.5	29.6	21.4
Antananarivo	42.4	52.0	43.3	...	15.9	23.0	17.5
Fianarantsoa	64.9	83.1	55.8	...	22.4	42.0	25.2
Taomasina	55.8	76.3	52.6	...	18.5	39.9	21.1
Mahajanga	37.3	68.2	65.2	...	11.6	23.2	25.3
Toliara	66.9	69.1	66.5	...	25.0	37.3	29.8
Antsiranana	49.5	27.0	31.3	...	14.3	6.2	7.8
Rural Poverty							
Total	74.5	76.0	76.7	74.9	33.1	34.7	36.1
Antananarivo	76.2	72.1	69.3	...	31.6	31.5	29.5
Fianarantsoa	75.3	73.6	85.9	...	35.3	30.1	43.1
Taomasina	81.1	80.8	76.4	...	36.0	39.2	35.7
Mahajanga	56.7	75.1	78.8	...	20.2	30.6	39.4
Toliara	84.2	84.9	73.1	...	46.5	48.5	34.8
Antsiranana	63.7	69.5	80.6	...	24.5	27.5	36.7
National Poverty	70.0	73.3	71.3	69.2	30.3	33.6	32.9

Source: INSTAT, Cornell University and World Bank staff estimates from household survey data.

[1] Headcount measures the share of population with per capita consumption below the poverty line. Based on a household surveys conducted in 1993, 1997, 1999, and 2001, the poor are defined as those who spent FMG 313,945 (US$164) per capita or less in 1993. Depth of poverty measures by how much consumption on average falls short of the poverty line. Poverty is reported for the six provinces of the country. For each province, poverty is measured separately in the main urban center and in the rural areas.

Table 15. Madagascar: Basic Social and Demographic Indicators [1]

Land area (square kilometers)	581,540
Population	
Total (in millions) (2001)	16.0
Urban population (percent of total)	30.0
Population density (people per sq. km.)	26.7
Population density, rural (people per sq. km. of arable land) (1998)	407.6
Population growth (annual percentage)	3.1
GNI per capita (in U.S. dollars, *World Bank Atlas*method, 2001)	260.0
Life expectancy at birth (in years) (2001)	
Overall	55.0
Women	55.8
Men	52.8
Crude birth rate (per 1,000) (1999)	40.7
Crude death rate (per 1,000) (1999)	12.1
Fertility rate (percent) (1999)	5.4
Infant mortality rate (per 1,000) (2001)	92.0
Child (under 5 years) mortality rate (per 1,000)	143.9
Stunting among children under 5 years (1997)	48.3
Education	
Illiteracy rate, adult total (percentage of people over 15) (2001)	33.0
Primary education, pupils (in thousands) (1998)	1,889.9
Secondary education, general pupils (in thousands) (1997)	356.6
Secondary education, vocational pupils (in thousands) (1992)	8.1
Primary school gross enrollment rate (percentage of relevant age group) (2001)	102.0
Secondary school gross enrollment rate (percentage of relevant age group) (1999) [2]	19.4
Tertiary school gross enrollment rate (percentage of relevant age group) (1995)	2.2
Health	
Hospital beds (per 1,000) (1999)	0.5
Physicians (per 1,000) (1999) [2]	0.1
Safe water (percentage of population with access) (2001)	47.0
Rural	31.0
Urban	85.0
Sanitation (percentage of population with access) (1999)	
Rural	30.0
Urban	70.0
Child immunization (under 12 months, percent) (1999)	
DPT	54.7
Measles	55.1
HIV prevalence (1999) [2]	0.15

Sources: World Bank, *World Development Indicators*2001, available on CD-ROM; and Malagasy authorities.

[1] Most recent estimates available, unless otherwise indicated.

[2] Source is the authorities' interim PRSP.

Antananarivo, December 4, 2002

Mr. Horst Köhler
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Mr. Köhler:

1. The attached Memorandum on Economic and Financial Policies describes the policies and measures that the government of Madagascar has adopted and pursued since July 2002, in the wake of the severe political crisis that affected the country in the first half of this year, and describes in detail Madagascar's economic and financial policy for the remainder of this year and for 2003. The government requests that this document serves as the basis for the Fund's completion of the second review under the Poverty Reduction and Growth Facility (PRGF) approved on March 1, 2001. The government requests a waiver for nonobservance of the performance criteria for end-December 2001 regarding the net domestic assets of the central bank, net domestic financing of the government, and fiscal revenue, in view of the steps the government has taken since June to strengthen fiscal management and establish principles of good governance at all levels, which we believe are key to establishing a strong foundation for growth. The government also requests a waiver for the accumulation of payments arrears on the external debt in early 2002, owing to the freeze of external reserves of the central bank; these arrears have been settled in June-July, as soon as the reserves were released.

2. Given the interruption in the implementation of the PRGF-supported program during the first half of 2002, the government of Madagascar requests that the arrangement be extended through end-November 2004. The third review of the arrangement is expected to be completed by end-May 2003, with subsequent reviews occurring every six months. The government of Madagascar will continue to provide the Fund with any information deemed necessary to monitor program implementation.

3. The government wishes to request additional interim assistance under the enhanced HIPC Initiative for the period January 1, 2003-December 31, 2003.

4. The government of Madagascar believes that the policies described in the attached Memorandum are sufficient to achieve the program objectives, but is prepared to take any additional steps that may become necessary to achieve these objectives.

Sincerely yours,

Benjamin Andriamparany Radavidson
Minister of Economy, Finance, and the Budget

MADAGASCAR

Memorandum on Economic and Financial Policies for 2002-2003

December 4, 2002

I. INTRODUCTION AND ECONOMIC AND FINANCIAL DEVELOPMENTS IN 2001

1. For several years, Madagascar has been implementing a program of macroeconomic and structural reforms aimed at restoring domestic and external viability, boosting growth, and reducing poverty. After achieving favorable results in terms of growth and reduction of domestic and external imbalances in the 1997-2000 period, the authorities adopted a medium-term economic and financial program supported by a three-year arrangement under the Poverty Reduction and Growth Facility (PRGF). Following the first review in December 2001, the implementation of the program was interrupted by a serious political crisis. With the resolution of the crisis in July 2002, the new government began a recovery effort, with donors assistance, within a revamped framework of good governance and enhanced participation, bolstered by reforms designed to accelerate the process of growth and poverty reduction.

2. The economic and financial program for 2001 yielded satisfactory macroeconomic results. Real GDP growth reached 6 percent, following an average growth rate of 4.2 percent in the preceding four years. The year-on-year inflation rate, measured by the consumer price index (CPI), fell to 4.8 percent at end-2001. The external current account deficit (including official transfers) fell from 5.6 percent of GDP in 2000 to 1.3 percent of GDP in 2001, owing to a 20 percent export growth in SDR terms, including a sharp rise in traditional exports and a twofold increase in the Export Processing Zone's (EPZ) exports, which were boosted by the entry into force of the U.S. African Growth and Opportunity Act (AGOA) in early 2001. The central bank's external reserves increased from the equivalent of 10.2 weeks of imports of goods and services at end-2000 to 14.4 weeks at end-2001, substantially exceeding program targets.

3. Despite favorable results in terms of growth, revenue developments in 2001 were disappointing, especially in the second half of the year. In particular, fiscal revenue in 2001 amounted to only 10 percent of GDP (FMG 3,029 billion) in contrast to the program target of 11.9 percent of GDP. The shortfall was mainly due to customs revenue, and can be attributed to the impact on custom revenue of the unexpected appreciation of the Malagasy franc, administrative weaknesses especially in secondary ports, identified frauds with an estimated cost of FMG 60 billion in lost revenue (0.2 percent of GDP), and to the poor performance of the tax receipts on petroleum products (FMG 272 billion instead of the projected FMG 443 billion).

4. On the expenditure side, current spending on goods and services exceeded program projections by FMG 34 billion (0.1 percent of GDP), entirely on account of expenditure through the presidential special funds (FMG 171 billion instead of the projected FMG 2.8

billion); other current spending (other than HIPC initiative financed) remained below budget by FMG 90 billion, while the priority HIPC-financed current expenditure were below budget by FMG 44 billion (FMG 82 billion executed as against FMG 126 billion programmed). However, both the domestically- and externally- financed components of capital expenditure remained well below the projections, with total capital expenditures reaching FMG 2,181 billion (7.2 percent of GDP) instead of the projected FMG 2,995 billion (10 percent of GDP). Consequently, the budget deficit (on a commitment basis, and excluding grants), despite having widened from 6.4 percent of GDP in 2000 to 8.1 percent of GDP in 2001, remained below the programmed amount.

5. With regard to expenditure for structural reforms, in 2001 an appropriation of FMG 100 billion for petroleum product subsidies was used to help SOLIMA pay customs duties (FMG 50 billion) and domestic VAT (FMG 15 billion) and to repay a portion of the central bank (BCM) advances for petroleum purchases (FMG 35 billion). Despite this subsidy, SOLIMA's debt to the BCM continued to grow in 2001, allowing the company to reduce its debt toward private suppliers; this debt amounts at present to US$51 million. An audit of the accounts of SOLIMA for 2000 and 2001 is under way (see para 29). Privatization receipts fell below the revised estimates (FMG 104 billion instead of FMG 200 billion), because of lower than expected receipts from the sale of SOLIMA storage facilities and service stations.

6. The reduction of domestic arrears in 2001 amounted to FMG 27 billion instead of the FMG 115 billion programmed. At December 31, 2001, payments outstanding at the treasury totaled FMG 424 billion (1.4 percent of GDP) and VAT credits refunds payable by the government amounted to FMG 70 billion, including FMG 28 billion due to EPZ companies. Owing to the shortfall in revenue, privatization receipts, and external budgetary support (SDR 50 million, or 1.4 percent of GDP), the government's domestic borrowing in 2001 was larger than programmed by the equivalent of 0.7 percent of GDP (FMG 658 billion compared with FMG 452 billion programmed).

7. All the performance criteria and quantitative benchmarks for end-March, end-June, and end-September 2001 were met, with the exception of fiscal revenue for each period. The following performance criteria for end-December 2001 were not met: net domestic assets of the central bank, as its advances to SOLIMA were not repaid as expected; domestic financing of the government, partly on account of a large shortfall in external assistance; and fiscal revenue for the reasons indicated above. However, the performance criterion pertaining to the net foreign assets of the central bank was met by a sizable margin. All of the 2001 structural performance criteria and benchmarks were met, with the exception of the benchmark concerning the entry in operation of the customs software system ASYCUDA 3++, which was delayed because technical assistance was not received in time (Tables 1 and 2, attached).

II. ECONOMIC DEVELOPMENTS IN THE FIRST PART OF 2002

8. The crisis triggered by the presidential elections of December 2001 brought the economy to a standstill, as the country was divided by roadblocks until end-June. Prices skyrocketed in the first six months of 2002 as a result of shortages of oil, electricity, and certain essential goods, and the blockade of the country's interior severely hampered production in the EPZ and in the secondary and tertiary sectors; some 80,000 workers were temporarily laid off. Tourism ground to a complete halt. The international reserves of the central bank were frozen from March to July by key depository institutions, leading to the closure of the interbank foreign exchange market. According to surveys of the EPZ, industrial production declined by about 80 percent in the first six months of 2002 compared with the same period in 2001; the latest full-year estimates for 2002 indicate that real GDP could fall by about 12 percent. Between December 2001 and May 2002 the consumer price index rose by 21 percent, reflecting a surge in transportation and food prices. When fuel again became available in June, prices started to fall. From May to September, the CPI declined by 6.2 percent; by December, inflation on a year-on-year basis is projected to decline to 12 percent, whereas the GDP deflator is projected to rise in 2002 by about 15 percent. The crisis has brought about an increase in poverty, a sharp fall in school enrollment and in the use of basic health services. To counter these trends, the government has adopted specific measures in September (see para. 18). Donors have intervened with additional humanitarian aid, in particular with free distribution of medicines.

9. The crisis seriously weakened the financial position of most private and public enterprises (especially Air Madagascar and the electricity and water company JIRAMA). The share of nonperforming loans in commercial banks' portfolios increased substantially in the first six months of 2002 (see para. 26).

10. Budgetary revenue fell sharply during the crisis owing to the contraction of economic activity, employment, and imports. In the first six months of the year, revenue totaled FMG 857 billion, a decrease of 44 percent from the same period in 2001. In particular, customs revenue amounted to FMG 333 billion, compared with FMG 766 billion in the same period of 2001. In the July-September period, the pace of both customs revenue and domestic tax receipts increased.

11. Indicative benchmarks for end-March 2002 were established under the PRGF-supported program. Preliminary results indicate that the benchmarks for net foreign assets and net domestic assets of the central bank and domestic financing of the government were met, whereas the benchmark for fiscal revenue was not observed. Because of the intense pressure facing the treasury in the first quarter and the freezing of external reserves, arrears towards certain multilateral and bilateral creditors were accumulated, resulting in a breach of the continued performance criterion on external arrears; all of these arrears were subsequently settled in June and July 2002.

12. In the first six months of the year, affected by the crisis, the authorities have not been able to implement the budget for 2002 , approved by parliament in December 2001, including the HIPC budget. Wages and pensions were paid regularly and significant resources were allocated for military operations, whereas other operating expenditures were kept to a minimum. Outstanding payment orders at the treasury at end-2001 (FMG 424 billion) could not be settled as planned in early 2002. Moreover, VAT credits refunds owed to enterprises continued to rise in the first part of the year, so that by end-September VAT arrears to EPZ companies and other companies amounted to FMG 97.5 billion and FMG 67.5 billion, respectively. A total of FMG 40 billion was paid to export processing companies in early October 2002, and the remainder of 57 billion was repaid in the first half of November. VAT credits of ordinary enterprises were repaid starting in November, and the process will be completed before end-December.

III. The Program for the Last Quarter of 2002 and for 2003

A. Objectives and Priority Actions for 2002

13. Following the reunification of the country in June 2002 and the removal of all road-blocks, the government devoted all its energies to overcoming the crisis and introducing far-reaching reforms aimed at achieving good governance and transparency. This effort is expected to restore the confidence of economic agents and users of public services, as well as pave the way for equitable and sustainable growth that will benefit the entire population and substantially reduce poverty. The central role of good governance in the country's development was underscored in the government's message to the donors community at the Friends of Madagascar meeting in Paris on July 26, 2002. The government is aware of the difficult challenges that it faces in seeking to revive the economy and reversing the effects of the crisis, but is confident that with appropriate economic policies, determined actions to ensure good governance, and donor support, it will be able to secure a solid recovery and sustained growth beginning in 2003, in a framework of financial stability. The incidence of poverty, which rose in 2002 because of the economic consequences of the crisis and the loss of jobs, is expected to fall again with new job creation and the efforts underway to speed up disbursements under several community-based development projects, which benefit from foreign assistance.

14. To promote the recovery and assist economic agents who sustained heavy losses and/or lost their working capital during the crisis, the government decided in July to introduce a series of fiscal measures, that were implemented over the following months. These temporary measures include: allowing the payment of the corporate income tax (IBS) on 2001 earnings to be spread out over the year 2002; suspension of the IBS advance payment for 2002; and suspension of the 3 percent IBS advance payment at customs. Also with a view to improving the cash flow situation of companies, a major effort was launched in August to accelerate the settlement of outstanding payment orders at the treasury, as well as the reimbursement of VAT credits. As a result, outstanding payment orders at the treasury were reduced by FMG 300 billion (1 percent of GDP) between end-June and October 15, 2002, and were fully paid in November. Pending the finalization of a new mechanism regarding the

VAT obligations of the EPZ companies, that would allow to offset payments due on imports with credits on exports, a temporary measure has entered in effect at end-October which defers for three months the payment of VAT on imports. Moreover, to facilitate the operations of export processing enterprises and promote their integration with local production, including artisanal production, customs duties on textile sector inputs (fabrics, accessories, and production equipment) were eliminated effective November 7, by presidential decree.

15. The presidential decree of November 7 introduces important customs tariff reductions in order to promote economic recovery; thus the tariff on fertilizer, agricultural inputs, and farm equipment, and on iron and steel products, certain construction materials, cement and paper has been brought to zero. The tariff on certain equipment goods and raw materials has also been reduced, to the new maximum rate of 25 percent (previously 30 percent) or below. To offset partly the cost of these measures, estimated at FMG 28 billion on an annual basis (0.1 percent of GDP) the excises on cigarettes and motor oil have been raised.

16. To prevent delays in the payments by the government of duties and taxes on externally financed public procurement contracts, the procedures for the payment by the government of taxes, including the VAT, will be revised before end-January 2003. This new mechanism will be reviewed before end-June 2003 in consultation with the Fiscal Affairs Department of the Fund . New regulations will be adopted before end-June 2003, in consultation with the Fund's Fiscal Affairs Department, authorizing the deferment of the VAT payments obligations on imported capital goods. Measures have also been designed to help enterprises reconstitute their working capital; accordingly, a bank loan guarantee fund is being set up with donor assistance, which will begin operations in January 2003.

17. The government has also decided to make additional resources available to rural and urban municipalities using appropriations originally earmarked for regional districts. Accordingly, transfers to urban and rural municipalities amounting to FMG 29 billion were carried out before end-October. In 2003 these allocations will be increased to about FMG 80 billion.

18. The crisis severely affected the most vulnerable groups and reduced their possibility to access schools and health care centers. To counter this negative impact, the government has decided to waive school fees for a six month period starting in October. Health care and drugs provided in the public health centers have been set free of charge for a transitory six month period. The cost of these measures is estimated at FMG 63 billion (0.2 percent of GDP), and is covered by the HIPC budget.

B. Public Finance and Good Governance

19. Given the importance of repaying the large domestic arrears outstanding, and the need to bolster the financial position of public enterprises providing essential services, the government is aware of the need to be very prudent in managing expenditure for the remainder of the year. The latest estimates for 2002 indicate that budget revenue could total FMG 2,250 billion (7.3 percent of GDP, as against 10 percent of GDP in 2001), of which FMG 950 billion would come from customs and FMG 1,150 billion from domestic

taxes. Current expenditure will be limited to FMG 3,250 billion, or 10.5 percent of GDP, compared with 10.2 percent in 2001. Investment expenditure is estimated at FMG 1,150 billion, or 3.7 percent of GDP, of which FMG 910 billion is to be externally financed. The domestically financed investment expenditure component (FMG 242 billion) will be used primarily to pay the taxes and duties on externally financed projects, which is essential for successful project implementation. These amounts include additional expenditure of FMG 318 billion financed with the debt relief under the HIPC Initiative, with an allocation agreed with donors giving priority to education, health, nutrition, road maintenance, drinkable water, and crop protection. The budget deficit (on a commitment basis, excluding grants) is expected to be limited to 7.7 percent of GDP.

20. External budgetary assistance in 2002 is projected at US$105 million (encompassing the third tranche drawing of US$42.5 million under the World Bank Second Structural Adjustment Credit, SAC II, disbursements under the World Bank Emergency Economic Recovery Credit, EERC, of US$20 million, European Union disbursements of €35 million, French emergency assistance of €6 million, and aid from Mauritius of US$1 million); of the Bank EERC the equivalent of approximately US$20 million will be on lent to public enterprises undergoing reorganization pending their privatization (Air Madagascar, Réseau Nord de Chemins de Fer, and HASYMA). This budgetary assistance is additional to the World Bank disbursements already received in 2002 (second tranche of the SAC II totaling US$30 million in January 2002 and an additional tranche of US$10 million for cyclone damage in July 2002). Privatization receipts are expected to total FMG 50 billion, since the sale of the state telephone company TELMA is expected to be finalized in early 2003. In view of the expected assistance, net repayment of domestic arrears in 2002 could attain an amount close to FMG 200 billion, or 0.6 percent of GDP.

21. The government is determined to improve fiscal management at all levels and to introduce the principles of good governance in order to remedy past deficiencies. The key measures already taken include: (i) appointment of new managers in all customs offices; (ii) recovery of duties payable on imports in 2001; (iii) the audits by the State Inspectorate General of the 2001 expenditures through the special fund of the office of the president, finalized in October 2002, and of the 2001 HIPC expenditures; (iv) establishment of an anti-corruption board to help draft appropriate legislation in this area as well as create an anti-corruption agency. The National Statistical Institute has been put in charge of the preparation of a report on the physical execution of priority expenditure financed by the HIPC budget in 2002. In addition, the ongoing strengthening of control agencies such as the Audit Court (*Cour des Comptes)*, the Directorate-General for Expenditure Commitment Control (*Control des Dépenses Engagés, CDE)*, and the State Inspectorate-General (*Inspection Général de l'Etat)* will continue with donor assistance.

22. A wide-ranging effort will be undertaken to improve the efficiency of the customs administration, particularly to curtail fraud, while at the same time streamlining customs clearance procedures and minimizing unnecessary controls which are burdensome for economic operators. Accordingly, strict instructions have been given to customs agents to discontinue practices that slow down customs clearance. The computerization of customs

will be accelerated with the installation of ASYCUDA 3++ in all main customs offices. The new contract with a pre-shipment inspection company will be finalized by end-March 2003 and a timetable will be established for settling arrears under the previous contract with BIVAC, which expired in 2001.

23. The treasury continues its efforts to expedite the preparation of monthly treasury balances; the balances for the year 2000 will be completed by end-2002 and those for 2001 and 2002 will be prepared in 2003. Starting in early 2004, the monthly closing balances will be prepared on a timely basis. The delays in the preparation of the budget execution laws (*lois de règlement*) will be eliminated, and the draft budget execution law for 1999 will be forwarded to the Audit Court before end-2002. The draft budget execution laws for 2000 and 2001 will be submitted to the Audit Court in 2003.

24. To expedite the expenditure commitment procedures and increase the speed of budget execution, the CDE has established a one-stop window in each ministry, which either grants or denies approval for the commitment of expenditure within 48 hours. To improve budget execution at the expenditure verification and authorization stage, the provincial budget directorates will be strengthened with support from the World Bank and other donors. Quarterly budget execution reports, now limited to the Ministries of Education and Health, will be extended in 2003 to include the Ministries of Public Works, Rural Development, Water and Forests, and Justice. Quarterly execution reports will be prepared of the expenditures in the HIPC budget, starting with a report on 2002 expenditures, which will be finalized before end-March 2003. In addition, with World Bank assistance, the medium-term objective is to establish an integrated fiscal management system, based on reliable data reporting procedures.

C. Balance of Payments and External Debt

25. Regarding balance of payments developments in 2002, available information on EPZ enterprises indicates that business is gradually reviving, with 49 of 142 enterprises having resumed operations, at least partially. The pace of recovery will depend on the ability to obtain new purchase orders from foreign clients, after the interruption of business activity early in the year. Overall, exports could shrink by as much as 46 percent between 2001 and 2002, with a strong decline in EPZ exports. Vanilla exports are expected to contract by 16 percent because of a decrease in volume. Imports are recovering only gradually, including imports of petroleum products, as household consumption and business inventory rebuilding remain weak. According to provisional estimates, the current account deficit, including grants, could amount to 4.5 percent of GDP, compared with 1.3 percent in 2001. Despite the external assistance expected in the final months of the year, the central bank's net external reserves could contract by approximately SDR 30 million during the year, compared with a decrease of SDR 73 million in the first nine months of the year. The government is in the process of finalizing the bilateral agreement with Paris Club creditors, on the basis of the Agreed Minutes of March 2001.

D. Monetary Policy and the Banking System

26. The money supply remained stable in the first eight months of 2002 and the demand for bank credit was weak, including in the third quarter, leading to a 7.6 percent reduction in bank lending over the eight months. The demand for credit to the economy could revive in the final months of the year. To facilitate such a recovery, on October 21, 2002 the central bank lowered the required reserve ratio on demand deposits from 24 percent to 18 percent , and on time deposits from 3 percent to 2 percent. The treasury bills market reopened on October 23, 2002 and interest rates rose above the levels attained in January 2002 before the market closed (for four-week bills from 5.5 to 11 percent, for 12-week bills from 8.9 to 11.9 percent, and for 24 weeks bills from 9.1 to 12.7 percent). Money growth for the year 2002 is projected at 11.9 percent, which would imply a decrease in the velocity of circulation. During the year, the share of nonperforming loans in the banks' portfolios increased (from 9.3 percent of loans at end-2001 to 13.8 percent at end-August 2002), owing to the difficulties economic agents encountered during the crisis. This will necessitate additional provisioning by banks, negatively affecting their 2002 earnings.

27. The monetary authorities will continue to pursue a flexible exchange rate policy, and the central bank will intervene on the exchange market solely to achieve its external reserves objectives and to minimize temporary exchange rate fluctuations. In their exchange policy, the authorities will take account of export developments and of the pace of recovery of the Export Processing Zone's activity, and will strive to preserve the competitiveness of the Malagasy economy.

28. The central bank is in the process of implementing an action plan designed to strengthen its internal organization and controls. Accordingly, in the coming months the central bank will develop a risk-based plan of internal audits of its departments, will carry out by end-June 2003 an audit of its foreign assets management system, and, with Fund technical assistance, will strengthen the management of its foreign reserves. The central bank will strive to improve the presentation of its accounts, based on internationally accepted accounting principles. The Bank Supervision Commission will receive technical assistance for the establishment of an early warning system of banks management. The central bank's board of directors will meet before end-January 2003 to review and approve the 2000 and 2001 accounts of the institution, and the accounts will be published by end-February 2003.

29. SOLIMA's debts to the central bank amounted to US$52 million at end-August 2002, owing to the nonpayment of letters of credits for petroleum imports in 2000 and 2001. The 2003 Budget Law will provide for these debts to be assumed by the government, and a repayment schedule will be drawn up. SOLIMA's accounts for 2000 will be closed and examined by the company's auditors by end-December 2002, and the 2001 accounts by end-June 2003. Before end-2002 accounts will be prepared presenting the sources and uses of funds in 2001. The general meeting of the company's shareholders will examine the 2000 accounts before end- February 2003, and the 2001 accounts before end-July 2003.

30. A financial and operational audit of the postal checking center (*centre des cheques postaux - CCP*) will be undertaken by end-March 2003. The purpose of the audit will be to make recommendations on the management of CCPs, including separation of the funds of CCPs and the post office, and any other measures necessary to ensure the viability of the CCP system.

E. Structural Reforms

31. The weakening of the financial position of the major public enterprises, reflecting the crisis of early 2002 as well as serious management deficiencies, requires that a vigorous restructuring program be put in place for the key enterprises, aiming at opening up their capital and/or their privatization; these enterprises play a key role in transport and rural development. Regarding Air Madagascar, the government made recourse in June, in consultation with the World Bank, to a Lufthansa Consulting team , which in September concluded a two-year management contract with the company; the objective is to improve management efficiency and generate a positive cash flow, so as to permit the privatization of the company. Improvement in operating results will allow to reduce the debt burden. The government, for its part, will inject additional equity (equivalent to US$10 million in 2002 and US$7 million in 2003), and creditors are expected to approve debt reduction arrangements. At end-September 2002 a concession was granted to a new private company with government participation for operating the northern railroad system (Réseau Nord de Chemins de Fer). The main shareholder of the concession company is the South African firm COMAZAR. The contribution of the government for rehabilitation investments and severance pay will amount to FMG 55 billion in 2002 and FMG 32 billion in 2003. Negotiations with the prospective buyers of the telecommunications company TELMA on the terms of the sale agreement are underway, and the sale is scheduled to be completed in the first quarter of 2003. As for the cotton company HASYMA, decisions will be taken shortly on the strategy for opening up the company's capital, which has become urgent given its inadequate capital and the accumulation of debts, including to cotton farmers. The government will assume responsibility for settling the debts to farmers, amounting to FMG 13 billion in 2002 and FMG 10 billion in 2003. For the sugar sector, which is in urgent need of revamping following the steep declines in production in recent years, efforts are under way to achieve the structural rehabilitation of the sugar company SIRAMA, with government assistance to the company expected to total FMG 28 billion in 2003.

32. As the management of the electricity and water company JIRAMA has been seriously weakened by its inability to recover claims on public entities such as local governments and the university, as well as by the recent increase in the price of diesel oil, the priority is now to settle the company's arrears to fuel suppliers and improve its cash flow so as to ensure its proper functioning. This will necessitate (i) an appropriate tariff policy, which will reflect also the recent increase in gas oil prices; to that end a tariff study is underway, and a tariff adjustment will be introduced no later than end-February 2003; and (ii) the recovery of JIRAMA's claims on public entities (university, local governments), which will require government intervention in the framework of a cross arrears compensation arrangement with the oil companies. This arrangement will offset oil companies claims on JIRAMA, other state

enterprises, and the central government for gasoline and fuel consumption, with import duties and taxes payable for the first half of 2002. This offsetting arrangement has been concluded in early December 2002. The government will be attentive not to accumulate arrears on fuel consumption, while local authorities financial management will be strengthened, to avoid incurring new arrears toward JIRAMA. An operational audit of JIRAMA will be carried out in the coming months by a team of consultants, with World Bank assistance, who will issue comprehensive recommendations for managerial improvement. Moreover, to ensure that the electricity sector is properly managed and that the marketing of electricity produced by private operators is competitive and transparent, the electricity sector regulatory agency established by law will become fully operational during the month of January 2003.

F. Economic Growth and Fiscal and Monetary Objectives for 2003

33. The recovery of economic activity, including in the EPZ, and the resumption of investment (private and public) are expected to generate real GDP growth of approximately 7.8 percent in 2003. A sharp upturn is expected in the construction sector owing to the increased rate of execution of a number of externally financed projects including construction and rehabilitation. Consumer price inflation is expected to continue falling, to about 5 percent on a 12-month basis by end-2003. The increase in the GDP deflator in 2003 is projected at 3.8 percent. Exports are projected to increase by about 32 percent in SDR terms, particularly as a result of recovery in apparel production. A drop is expected in the vanilla export price, which could lead to a decrease in vanilla exports in value terms. Imports are expected to increase by approximately 32 percent in SDRs, mainly because of the recovery of investment. As a result, the external current account deficit (including grants) is projected to widen to 5.7 percent of GDP, and the central bank's net official reserves are expected to increase by about SDR 23 million, partly as a result of the expected recovery of foreign direct investment.

34. The 2003 Budget Law is under preparation; it will be adopted by presidential decree (*ordonnance*) before end-2002 and ratified by the National Assembly which will be elected on December 15, 2002. The budgetary framework has been designed taking into account the effort to strengthen tax and customs administration and the external assistance expected for projects and budgetary support. On the revenue side, the government intends to reduce evasion significantly by strengthening customs administration (introduction of ASYCUDA 3++; new contract with an inspection company; enhanced controls; cross checks with the domestic tax offices) and tax administration (prohibition of sales without invoices; cross checks). Customs receipts are expected to reach FMG 1,620 billion (an increase of 11.5 percent from 2001). Domestic tax receipts could reach FMG 1,890 billion, up from FMG 1,460 billion in 2001; this increase reflects in part larger VAT receipts because of the rapid growth of externally financed public investment. The collection of the unified tax on small businesses (*impôt synthétique*), which had been suspended in 2001, is projected to yield FMG 68 billion (0.2 percent of GDP). Total budgetary revenue is expected to amount to 10.5 percent of GDP, compared with 10 percent of GDP in 2001 and 11.7 percent in 2000. Revenue performance in the first half of the year will be analyzed in July 2003; should the annual target appear difficult to achieve, the government will consider the adoption of new

revenue measures, or will offset the expected revenue shortfall by curtailing from July new expenditure commitment.

35. Current expenditure will be maintained at a level equivalent to 10.2 percent of GDP as in 2001, including priority expenditure of approximately FMG 239 billion (0.7 percent of GDP) financed by debt relief under the HIPC Initiative (an additional FMG 124 billion in debt relief will be allocated to investment expenditure). The wage bill will reflect an increase in wages of 12 percent, and additional allowances for teachers in rural areas and for the security forces. Externally financed investment expenditure are projected at FMG 1,700 billion (4.9 percent of GDP, compared with 4.1 percent in 2001). Domestically financed investment expenditure are budgeted at FMG 800 billion (2.3 percent of GDP). Transfers to municipalities will be increased. The budget deficit (commitment basis, excluding grants) will decline to 7.4 percent of GDP, from 7.7 projected for 2002 and 8.1 percent in 2001.

36. Already identified external budgetary support (excluding projects financing) will amount to the equivalent of US$ 65 million, including US$30 million in World Bank emergency credit, and €35 million from the European Union; a residual gap equivalent to US$45 million could be covered by bilateral donors and the AfDB. PRGF disbursements from the IMF will be channeled through the central bank. Banking system credit and nonbank lending to the government will be small in view of the need for bank financing to revitalize the private sector. Privatization receipts are projected to reach FMG 133 billion, including the proceeds of the sale of TELMA. Within this financing framework, domestic payments arrears could be reduced by approximately FMG 300 billion or 1 percent of GDP.

37. The monetary policy objectives for 2003 are to reduce inflation while at the same time ensuring adequate expansion of credit to the private sector, which is essential for recovery. Increases in the central bank's external reserves and net bank credit to government would contribute to expanding the money supply by 4.7 percent and 3.6 percent, respectively. A 15 1/2 percent increase in credit to the economy (excluding the impact of the government assumption of central bank claims on SOLIMA) would be equivalent to 5.6 percent of beginning-period money supply, and would be compatible with a monetary expansion of 12.5 percent during the year, in line with the expected growth of nominal GDP.

G. Preparation of the Poverty Reduction Strategy Paper

38. The Poverty Reduction Strategy Paper (PRSP), currently under preparation, presents an in-depth diagnostic analysis of trends in poverty in recent years, the main focuses of the proposed poverty reduction strategy, the key medium-term objectives, and the costs of programs needed to achieve the objective. The action programs will be prioritized on the basis of the available financing, and all actions will be properly budgeted. The final content of the PRSP will be reviewed by a national workshop to be held in January 2003 in Antananarivo and will be submitted for discussion by the new National Assembly in its first session in early 2003, before being adopted by the government and forwarded to the donor community. The government hopes to be able to attain the completion point under the HIPC Initiative in early 2004, after one year of implementation of the PRSP.

IV. Program Monitoring

39. The program supported by the PRGF arrangement will be monitored through semi-annual reviews, quantitative and structural performance criteria, quantitative and structural benchmarks, and quarterly monitoring indicators. The third review of the program is to be completed by the Fund's Executive Board by end-May 2003 and will focus on observance of the performance criteria for end-December 2002 and on economic and financial developments in the final months of 2002 and the initial months of 2003. The fourth review is to be completed by the Fund's Executive Board by end-November 2003 and will focus on observance of the performance criteria for end-June 2003, economic and financial developments in 2003, and the macroeconomic and fiscal targets for 2004. The performance criteria established for end-December 2002 and end-June 2003 (see Table 3, attached) pertain to the BCM's net foreign and domestic assets, domestic financing of the budget deficit (bank financing, nonbank financing, deposits of treasury correspondents, privatization receipts, and domestic arrears), fiscal revenue, the nonaccumulation of external arrears, and a ceiling on nonconcessional external government borrowing. The targets for these variables for end-March and end-September 2003 constitute benchmarks for program monitoring. The provisional targets established for end-December 2003 for these variables will be revised during the third review.

40. The following structural performance criteria and benchmarks have been established (see Table 4, attached): (i) by end-June 2003 new regulations will be adopted, in consultation with the Fiscal Affairs Department of the Fund, introducing a system authorizing the deferment of the VAT payment obligation until the monthly declaration following the import; (ii) the treasury's monthly balances up to end-2001 will be prepared before end-June 2003; (iii) the draft budget execution laws for 2000 and 2001 will be submitted to the Audit Court by end-December 2003; (iv) an activity plan for the central bank's internal audit department will be drawn up by end-March 2003, together with an organizational chart defining how the internal audit department will report to the various organs of the bank; (v) an internal audit of the management of central bank reserves will be conducted by end-June 2003; (vi) the general shareholders meeting of the oil company SOLIMA will examine the accounts for 2000 before end-February 2003, and those for 2001 before end-July 2003. The measures mentioned in (i) and (iii) constitute performance criteria under the arrangement; the other measures constitute benchmarks, the nonobservance of which will trigger consultations with Fund staff.

41. The following measure will constitute a prior action for completing the second review under the PRGF arrangement with the IMF: the JIRAMA's debts to private sector petroleum suppliers will be offset with these suppliers tax obligations.

Table 1. Madagascar: Quantitative Performance Criteria and Benchmarks for the first year under the 2001-03 PRGF arrangement
(In billions of Malagasy francs, unless otherwise indicated)

	2001 1/												2002		
	March			June			September			December			Change from January 1 to March 31		
	Bench-mark	Adj.	Actual	Perfomance Criteria	Adj.	Actual	Bench-mark	Adj.	Actual	Perf. criteria	Adj.	Actual	Bench-mark	Adj.	Actual.
I. Quantitative benchmarks and performance criteria															
Ceiling on external arrears (in millions of SDRs) 2/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	4.6
Floor on net foreign assets (NFA) of the central bank 3/ 4/ 5/ 6/	239.1	31.4	131.7	202.6	-191.2	309.4	208.5	-233.9	304.3	513.6	274.2	674.4	-22.1	-96.8	-48.0
Ceiling on net domestic assets (NDA) of the central bank 5/ 6/ 8/	-93.7	114.0	-46.5	-333.0	60.8	-254.5	6.8	449.2	3.8	-279.2	-39.8	167.2	130.0	204.7	-130.5
Ceiling on domestic financing of the government 5/ 7/ 11/	101.2	171.8	171.3	140.6	239.6	-71.7	506.7	590.5	466.4	462.1	589.7	658.1	315.0	389.7	-157.5
Ceiling on contracting or guaranteeing of external debt on nonconcessional terms 9/ 10/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Floor on tax revenue	736.5	736.5	610.2	1,672.1	1,672.1	1,536.0	2,572.9	2,572.9	2,155.4	3,470.0	3470.0	2906.4	710.0	710.0	424.3
II. Indicative limits															
Ceiling on reserve money	141.9	141.9	34.8	-134.0	-134.0	-2.9	211.8	211.8	280.4	225.7	225.7	805.5	108.0	108.0	-215.1
Ceiling on broad money (including foreign currency deposits) (M3)	95.6	95.6	140.8	-163.3	-163.3	477.8	328.0	328.0	623.1	958.5	958.5	1,440.9	161.0	161.0	130.9
III. Memorandum items: 1/															
Budget support grants and loans (in millions of SDRs)	23.7	...	13.7	59.7	...	43.0	72.3	...	43.0	92.5	...	43.0	0.0	...	0.0
Cash debt service (in millions of SDRs)	8.1	...	8.2	18.5	...	15.8	26.9	...	21.0	39.0	...	39.0	6.1	...	15.1
Privatization proceeds	142.0	...	4.9	315.9	...	21.1	390.9	...	32.3	215.9	...	104.1	12.0	...	10.8
Privatization related costs	29.5		61.0	81.0		61.0	183.6	...	68.5	191.9	...	70.5	20.0	...	...

1/ Cumulative change since the beginning of each year.

2/ Excludes all debt service outstanding that is subject to rescheduling. During the program period, the government will not accumulate any new arrears.

3/ Net foreign assets of the Central Bank of Madagascar (BCM) are defined as gross reserves minus all foreign liabilities of the BCM, both long and short term, including use of Fund credit.

4/ This amount will be valued at the exchange rates that were set for the purposes of this program.

5/ The floor on NFA of the central bank will be adjusted upward, and the ceilings on NDA of the central bank and on domestic financing of the government will be reduced, by the amount of any excess disbursements of balance of payments assistance relative to the cumulative timetable indicated in III. In case of a shortfall in balance of payments assistance, the floor on NFA of the central bank will be reduced by the amount of the shortfall, up to a maximum of SDR 25 million at end March 2001, and SDR 30 million at end June, September and December 2001, and the ceilings on NDA of the central bank and on net domestic financing of the government will be raised on a cumulative basis by the same amount.

6/ NFA and NDA of the central bank will be adjusted for any deviation from programmed amounts of privatization receipts from abroad, net of privatization-related outlays. In case of a shortfall in net privatization receipts, the downward adjustment of the NFA (and the upward adjustment of the NDA) will be capped at the equivalent of SDR 40 million.

7/ The ceiling on domestic financing of the government will be adjusted for deviations from programmed privatization-related outlays; the ceiling is defined to exclude the impact of foreign currency adjustments on bank financing of government.

8/ NDA of the central bank are defined to exclude the foreign currency adjustment.

9/ Excluding normal import-related credits.

10/ Defined as debt with concessionality level of less than 35 percent, calculated using the 10-year average of the OECD's commercial interest reference rate (CIRR)-based discount rate for loans of a maturity greater than 15 years, and the 6-month average CIRR-based discount rates for maturities below 15 years.

11/ Defined as excluding the assumption by the government of debt of the state petroleum company SOLIMA toward the BCM at the time of the final closing of SOLIMA operations.

Table 2. Status of Structural Performance Criteria and Benchmarks
Under the First Annual Program (2001)
Under the PRGF

Prior Actions, Benchmarks, and Criteria	Timing	Status
I. The following **structural performance criteria** will be used to monitor the 2001 annual program:		
a. The new "ASYCUDA 2.7" customs computer system will become operational at the three main customs offices.	By June 30, 2001	Completed on time
b. The adoption by the Council of Ministers of a bill to revise upward the mining royalty based on the value of the first transaction, and lower the excise tax.	By end-2001	Done
c. The treasury computer system, designed to centralize each month the accounts of the 22 main treasury offices, will be operational.	By end-November 2001	Done
II. The following **structural benchmarks** will be used to monitor the 2001 annual program:		
a. A study on the improvement in the operations of the State Inspector General (IGE) will be completed, and implemented during the second half of the year.	No later than end-June 2001	Study completed on time
b. The separation of the functions of the Chairman of the Central Procurement Committee (*Commission Centrale des Marchés*) and the Director General of Expenditure Commitment Control will become effective.	By June 30, 2001	Implemented on time
c. In the Directorate General of Customs, the "ASYCUDA 3 plus plus" system will be installed in the three most important offices.	By end-September 2001	Delayed
d. In the Directorate General of Customs, the "ASYCUDA 3 plus plus" system will be installed in four other offices.	By end-December 2001	Delayed

Table 3. Madagascar: Quantitative Performance Criteria and Benchmarks for 2002-03 under the PRGF arrangement
(In billions of Malagasy francs, unless otherwise indicated)

	2002	2003 1/			
	December Performance Criteria 1/	March Benchmark	June Performance Criteria	September Benchmark	December Indicative
I. Quantitative benchmarks and performance criteria					
Ceiling on external arrears (in millions of SDRs) 2/	0.0	0.0	0.0	0.0	0.0
Floor on net foreign assets (NFA) of the central bank 3/ 4/ 5/ 6/	-142.3	-88.6	-67.6	186.1	314.0
Ceiling on net domestic assets (NDA) of the central bank 5/ 6/ 8/	707.7	8.3	-60.0	135.8	246.0
Ceiling on domestic financing of the government 5/ 7/ 11/	530.9	182.8	-46.3	122.6	157.2
Ceiling on contracting or guaranteeing of external debt on nonconcessional terms 9/ 10/	0.0	0.0	0.0	0.0	0.0
Floor on tax revenue	2,162.3	755.0	1,700.0	2,480.0	3,509.0
II. Indicative limits					
Ceiling on reserve money	415.3	-110.2	-185.1	236.0	440.0
Ceiling on broad money (including foreign currency deposits) (M3)	875.1	306.1	263.5	791.6	1,025.1
III. Memorandum items: 1/					
Budget support grants and loans (in millions of SDRs)	110.4	11.4	68.0	82.5	82.5
Cash debt service (in millions of SDRs)	38.3	6.0	17.9	25.4	41.9
Privatization proceeds	49.4	96.4	117.8	130.6	132.9
Privatization related costs	9.5	10.0	20.0	25.0	30.0

1/ Cumulative change since the beginning of each year.

2/ Excludes all debt service outstanding that is subject to rescheduling. During the program period, the government will not accumulate any new arrears.

3/ Net foreign assets of the Central Bank of Madagascar (BCM) are defined as gross reserves minus all foreign liabilities of the BCM, both long and short term, including use of Fund credit.

4/ This amount will be valued at the exchange rates that were set for the purposes of this program.

5/ The floor on NFA of the central bank will be adjusted upward, and the ceilings on NDA of the central bank and on domestic financing of the government will be reduced, by the amount of any excess disbursements of balance of payments assistance relative to the cumulative timetable indicated in III. In case of a shortfall in balance of payments assistance at end-December 2002, and end-March, June, September and December 2003 , the floor on NFA of the central bank will be reduced by the amount of the shortfall, up to a maximum of SDR 40 million at end-December 2002, SDR 12 million at end-March 2003, SDR 45 million at end-June 2002, and SDR 55 million at end-September and end-December 2003, and the ceilings on NDA of the central bank and on net domestic financing of the government will be raised on a cumulative basis by the same amount.

6/ NFA and NDA of the central bank will be adjusted for any deviation from programmed amounts of privatization receipts from abroad, net of privatization-related outlays. In case of a shortfall in net privatization receipts, the downward adjustment of the NFA (and the upward adjustment of the NDA) will be capped at the equivalent of SDR 5 million for 2002; for end-March, June, September and December 2003, the adjustment will be capped at the equivalent of SDR 10 million.

7/ The ceiling on domestic financing of the government will be adjusted for deviations from programmed privatization-related outlays; the ceiling is defined to exclude the impact of foreign currency adjustments on bank financing of government.

8/ NDA of the central bank are defined to exclude the foreign currency adjustment.

9/ Excluding normal import-related credits.

10/ Defined as debt with concessionality level of less than 35 percent, calculated using the 10-year average of the OECD's commercial interest reference rate (CIRR)-based discount rate for loans of a maturity greater than 15 years, and the 6-month average CIRR-based discount rates for maturities below 15 years.

11/ Defined as excluding the assumption by the government of debt of the state petroleum company SOLIMA toward the BCM at the time of the final closing of SOLIMA operations.

Table 4. Performance Criteria, Structural Benchmarks, and Prior Actions Under the 2002/03 PRGF Supported Program

I. The following **structural performance criteria** will be used to monitor the 2002/03 annual program:

a. By end-June 2003 new regulations will be adopted, in consultation with the Fiscal Affairs Department of the Fund, introducing a system authorizing the deferment of the VAT payment obligation until the monthly declaration following the import (MEFP, para 16).
b. The draft budget execution laws for 2000 and 2001 will be submitted to the Audit Court by end-December 2003 (MEFP, para 23).

II. The following **structural benchmarks** will be used to monitor the 2002/03 annual program:

a. The Treasury's monthly balances up to end 2001 will be prepared before end-June 2003.
b. An activity plan for the central bank's internal audit department will be drawn up by end-March 2003, together with an organizational chart defining how the internal audit department will report to the various organs of the bank;
c. An internal audit of the management of central bank reserves will be conducted by end-June 2003;
d. The general shareholders meeting of the oil company SOLIMA will examine the accounts for 2000 by end-February 2003 and those for 2001 by end-July 2003.

III. The following measure will constitute a **prior action** for completing the second review under the PRGF:

Offsetting of JIRAMA's debts to private sector petroleum suppliers with these suppliers tax obligations (MEFP, para 32);

MADAGASCAR

Technical Memorandum on Monitoring the 2002-2003 Program Supported by the Arrangement under the Poverty Reduction and Growth Facility (PRGF)

1. This technical memorandum defines the variables used to establish the quantitative performance criteria and benchmarks for the program, how they are calculated, and any adjustments deemed necessary. It also explains the monitoring variables, that is, external financed assistance and direct investment flows connected with the privatization of public enterprises. Unless otherwise indicated, in the case of stocks variables for end-December 2002 are expressed as cumulative variations from December 31, 2001, and in the case of flows as cumulative flows from January 1, 2002. Variables for 2003 are expressed as cumulated variations from December 31, 2002 in case of stocks, and cumulated flows from January 1, 2003 in case of flows. The objectives for end-March and end-September 2003 are benchmarks; those for end-December 2002 and end-June 2003 are performance criteria. Objectives for end-December 2003 are indicatives and will be revised during the third review of the program.

I. Quantitative Criteria [1]

A. Ceiling on External Payments Arrears

2. This variable is expressed in terms of the stock of arrears. There will be no net accumulation of new arrears, meaning that there should be nil variation over the period considered.[2] External payments arrears are defined as nonpayment in full of interest and principal obligations due to all non-resident creditors, excluding arrears resulting from nonpayment of debt service for which rescheduling negotiations are under way.

B. Ceiling on Nonconcessional External Borrowing [3]

Definition

3. The nonaccumulation of nonconcessional debt contracted or guaranteed by the government is a performance criterion to be observed at all times. Nonconcessional external debt is defined as having a grant element of less than 35 percent. Under the program, nonconcessional debt includes financial leasing and any other instrument giving rights to a current financial liability, under a contractual arrangement by the government of Madagascar or

[1] These criteria are performance criteria for end -December 2002 and end-June 2003 and benchmarks for end-March and end-September 2003.

[2] To be observed continuously.

[3] To be observed continuously.

guaranteed by the government of Madagascar, but excludes debt contracted under rescheduling agreements and normal import-related credits of less than one year. A definition of debt is contained in point 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt, adopted by the Executive Board, on August 24, 2000. To this definition must be added all commitments contracted or guaranteed for which value has not been received.

Calculation method

4. Calculation of the degree of concessionality of new external borrowing is based on the 10-year average of the OECD's commercial interest reference rate (CIRR) for loans with maturities greater than 15 years and the six-month average CIRR for loans maturing in less than 15 years.

C. Floor for Net Foreign Assets (NFA) of the Central Bank of Madagascar

Definition

5. NFA are defined as the difference between gross international reserves and all foreign liabilities of the Central Bank of Madagascar (BCM), including debt to the IMF and other short- and long-term liabilities of the BCM. Gross international reserves are defined as reserve assets readily available to and controlled by the BCM for direct financing of payments imbalances, excluding assets that are pledged, or collateralized, or otherwise encumbered.

Calculation method

6. For purposes of calculating this criterion, NFA must be converted into Malagasy Francs (FMG) at the end-of-period exchange rates for the reference period established in the program (program exchange rate).

D. Ceiling on Net Domestic Assets (NDA) of the Central Bank of Madagascar

Definition

7. The BCM's NDA include net credit to the government, credit to enterprises and individuals, claims on banks, liabilities to banks in the form of central bank deposit auctions (*appels d'offres négatifs*), and the other items net, excluding the foreign exchange adjustment item.

8. Foreign exchange deposits must be converted into FMG at the end-of-period program exchange rate.

E. Ceiling on the Net Domestic Financing Requirements of the Central Government (CG)

Definition

9. Net domestic financing requirements of the central government are defined as the sum of (a) the variation in the net claims on the central government of the BCM, the commercial banks, the nonbanking system, and treasury correspondents; (b) domestic or foreign receipts from privatization operations as defined in Section III-B, paragraph 22 below; and (c) the variation in central government domestic or external payments[4] arrears. Central government (CG) corresponds to the scope of operations of the treasury as indicated in the General treasury Operations table (*Opérations globales du Trésor, or* OGT) .The change in deposits of the treasury correspondents (*correspondants du Trésor)* is considered a component of domestic financing.

10. The variation in domestic payments arrears consists of the amount to be recommitted and net payments delays (clearings, items in process of payment, expenditure committed but with no payments order issued), as defined in the OGT.

11. Net bank claims consist of BCM and commercial bank claims on the CG, including auctioned treasury bills (BTAs), and other treasury bills and liabilities, net of CG deposits with the BCM and commercial banks, including foreign currency deposits. The change in net bank claims is defined excluding the impact of exchange rate changes on net bank claims on the government.

12. Nonbank claims consist of BTAs and other treasury bills (BTs) and bonds placed with nonbank institutions and the public. The valuation of nonbank claims is based on the change in outstanding conventional treasury bills (maturities of 1 to 5 years), auctioned treasury bills (maturities of 1 month to 3 years), and outstanding domestic government loans.

Calculation method

13. Deposits and debt to the BCM in foreign exchange must be converted into FMG at the end of period program exchange rate.

14. BTAs must be posted at their net value at time of issue.

[4] These external payments arrears are defined as the amount of gross payments arrears less arrears eligible for debt relief, that is, the amount of arrears that must eventually be settled in cash.

F. Floor on Tax Revenue

15. Tax revenue includes that received by the treasury, but also suspense items, including those related to the public investment program.

II. Indicative Limits or Ceilings

A. Ceiling on Reserve Money

Definition

16. Reserve money consists of notes and coins issued and demand deposits of commercial banks with the BCM (including both required and excess reserves).

17. Central bank deposit auctions (*appels d'offres négatifs*) are excluded from reserve money and are classified in NDA.

B. Ceiling on Broad Money

Definition

18. Broad money (M3) includes notes and coins in circulation, demand and time deposits with commercial banks, including foreign currency deposits of residents, and bonds issued by banks.

Calculation method

19. Foreign currency deposits must be converted into FMG at the end-of-period exchange rates for the reference period established in the program.

III. Monitoring Variables and Memorandum Items

A. Projected Balance of Payments Assistance

Definition

20. External financial assistance is defined as loans and grants (nonproject) provided as structural adjustment financing and resulting in funds available to the treasury. It excludes the assistance that gives rise to counterpart funds for the treasury with a delay longer than one year.

Calculation method

21. Financial assistance in foreign exchange must be converted into FMG at the program exchange rate. Assistance in kind must be posted when the counterpart funds are deposited with the treasury.

B. Projected Investment Flows Connected with the Privatization of Public Enterprises

Definition

22. The cost of privatization operations is included above the line in central government operations. Apart from covering reform-related costs, gross receipts from the privatization of public enterprises (PEs) will be used to reduce outstanding domestic debt.

IV. Adjusters

A. Excess/Shortfall in External Financial Assistance

23. In the case of excess net external financing (external financial assistance less public debt service on a cash basis) over the amount programmed (i) the floor on the BCM's NFA will adjusted upward; (ii) the ceiling on the BCM's NDA will be adjusted downward (the adjustment will be converted into FMG at the exchange rate used in the operation); and (iii) the ceiling on the net domestic financing requirements of the central government (Section I-E) will be adjusted downward (the adjustment will be converted into FMG at the exchange rate used in the operation).

24. In the case of a shortfall in net external financing at end-December 2002, against the programmed amount, and at end-March, end-June, end-September, and end–December 2003, the floors and ceilings will be adjusted as follows: by a maximum of SDR 40 million for the year 2002; by a maximum of SDR 12 million for the first quarter 2003; by a maximum of SDR 45 million for the first half of 2003; by a maximum of SDR 55 million for the first nine months of 2003 and for the full year 2003, according to the following method: (i) the floor on the BCM's NFA will be adjusted downward by the amount indicated above; (ii) the ceiling on the BCM's NDA will be adjusted upward by the same amount (the adjustment will be converted at the program exchange rate); and (iii) the ceiling on the central government's net domestic financing requirements (Section I-E) will be adjusted upward and capped at the above-mentioned maximum amount (the adjustment will be converted to FMG at the program exchange rate) .

B. Privatization-Related Transactions

25. Adjustments will be made for any deviation in (a) privatization receipts; and (b) current privatization-related expenditure. The floor on net foreign assets for end-December 2002 will be adjusted upward or downward by a maximum of SDR 12 million from the programmed floor if disbursed foreign resources from privatizations net of (b) are

higher or lower than programmed. The adjustment will be limited to a maximum of SDR 5 million for the periods from end-2002 to end- March, end-June, end-September and end-December 2003. Similarly, the BCM's NDA will be adjusted downward or upward (at the average exchange rate of the pertinent quarter). The ceiling on domestic government financing will be adjusted to take account of any discrepancies between actual privatization-related expenditures and those programmed (upward adjustment if expenditure exceeds the amount programmed and downward, in the opposite case, up to the difference reported).

C. Program Exchange Rate

26. Amounts of external assistance and debt service denominated in SDRs will be converted into FMG at the exchanged rate of FMG 8,972= SDR 1 for the fourth quarter of 2002 and at the FMG/SDR rate respectively of 9,108, 9,240, 9,372, 9,514 for each of the four quarters of 2003. Corresponding amounts denominated in US$ and Euros will be converted in FMGs applying the rate of 1.32 US dollars per SDR and 0.98 US dollars per Euro, and the FMG/SDR rate indicated above.

V. Consultations with Fund Staff on the Performance Criterion for NFA and the Broad Money Benchmark

27. In case that demand for money is stronger than expected and the exchange rate appreciates, the central bank should intervene on the interbank foreign exchange market (MID) to offset this appreciation, taking into account programmed limits (floor/ceiling) on the accumulation of net foreign assets and the level of broad money. Given the program's target, if broad money growth since end-December 2002 exceeds 15 percent on an annual basis, and/or if the level of net foreign assets exceeds the programmed level by more than 5 percent of broad money at end-2002, the authorities will consult Fund staff on measures to be taken in the context of exchange market and monetary policy management.

VI. Information and Data to be Supplied to Fund Staff

28. The Malagasy authorities will provide Fund staff with the following information and data according to the schedule provided, either directly (e-mail or facsimile) or through the Fund's resident mission.

A. The Central Bank of Madagascar will report the following statistics

29. Monthly:

- market results of treasury bill auctions, including the bid level, the bids accepted or rejected, and the level of interest rates;
- data on the secondary treasury bill market, including volumes of transactions and yields;

- information on monetary developments, as required by the Statistics Department of the Fund (STA);
- monthly balances of the BCM and deposit money banks;
- classification of commercial bank loans by economic sector;
- money market operations and rates;
- changes in bank liquidity (required reserves and free reserves);
- the foreign exchange cash flow table, including foreign debt operations; and
- table of interbank foreign exchange operations on the interbank foreign exchange market (MID);

30. Quarterly:

- data on foreign trade (exports and imports).

B. The Ministry of Economy, Finance and the Budget will report, as appropriate, the following information:

31. Monthly:

- OGT data on a cash and commitment basis and the related tables;
- expenditure on structural reform;
- central government revenue and expenditure, including short-term treasury on-lending;
- treasury liabilities (statutory advances and operations on the treasury bill market);
- central government capital expenditure;
- external public debt operations (debt contracted and publicly guaranteed, settlement of external payments arrears, and operations of public enterprises) and debt service paid;
- traditional, modern and combined Malagasy price indices; and
- indicators of sectoral economic activity.

32. Moreover, information on important measures adopted by the government in the economic and social areas that would have an impact on program development, changes in legislation, including laws passed by the National Assembly and new rules established by the

Banking Supervision Commission (CSBF), and any other pertinent legislation will be reported to Fund staff on a timely basis for consultation or information, as appropriate.

Mr. Gaston Ravelojaona
Governor
Central Bank of Madagascar

Mr. Henri Bernard Razakariasa
Secretary General
Ministry of Economy, Finance,
and Budget

Madagascar: Relations with the Fund
(As of September 30, 2002)

I.	**Membership Status**: Joined 9/25/63; Article VIII		
II.	**General Resources Account**:	**SDR Millions**	**% Quota**
	Quota	122.20	100.00
	Fund holdings of currency	122.17	99.98
	Reserve position in Fund	0.03	0.02
III.	**SDR Department**:	**SDR Millions**	**% Allocation**
	Net cumulative allocation	19.27	100.00
	Holdings	0.01	0.07
IV.	**Outstanding Purchases and Loans**:	**SDR Millions**	**% Quota**
	Poverty Reduction and Growth Facility (PRGF) arrangements	100.02	81.85

V. **Financial Arrangements**:

Type	Approval Date	Expiration Date	Amount Approved (SDR millions)	Amount Drawn (SDR millions)
PRGF	03/01/01	02/29/04	79.43	22.69
ESAF/PRGF	11/27/96	11/30/00	81.36	78.68
ESAF	05/15/89	05/14/92	76.90	51.27

VI. **Projected Obligations to Fund Under the Repurchase Obligations Assumptions**[1]
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Overdue	Forthcoming				
	09/30/02	2002	2003	2004	2005	2006
Principal	0.00	1.36	5.42	5.42	8.14	16.87
Charges/interest	0.00	0.36	0.91	0.88	0.84	0.77
Total	0.00	1.72	6.33	6.30	8.98	17.64

[1] Repurchase Obligations: Repurchases in the credit tranches including the Compensatory Financing Facility, are to be completed in 3 ¼–5 years. Repurchases under the EFF are due in 4 ½–10 years.

VII. Implementation of HIPC Initiative:

Commitment of HIPC assistance	Enhanced framework
Decision point date	12/21/2000[2]
Assistance committed (NPV terms)[3]	end-1999
Total assistance (US$ Million)	814.00
Of which: Fund assistance (SDR million)	16.60
Completion point date	Floating
Delivery of Fund assistance (SDR million)	
Amount disbursed	2.12
Interim assistance	2.12
Completion point[4]	0.00
Amount applied against member's obligations (cumulative)	1.40

VIII. Safeguards Assessments:

Under the Fund's safeguards assessment policy, the Central Bank of Madagascar (CBM), is subject to a full Stage One safeguards assessment with respect to the PRGF arrangement, which was approved on March 1, 2001 and is scheduled to expire on February 29, 2004. An off-site safeguards assessment of the CBM was completed on November 12, 2001. The assessment concluded that an on-site assessment was not necessary, but identified certain weaknesses and made appropriate recommendations.

IX. Exchange System and Exchange Rate Arrangements:

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[2] World Bank Board the same day.

[3] NPV terms at the decision point under the enhanced framework.

[4] Under the enhanced HIPC initiative, the nominal amount of assistance disbursed will include an additional amount corresponding to interest on amounts committed but not disbursed during the interim period, calculated using the average return (during the interim period) on the investment of resources held by, or for, the benefit of the PRGF-HIPC Trust. After April 1982, when the peg to the French franc was discontinued, the exchange rate was managed with reference to a basket of ten currencies. However, by end-1991, the authorities

After April1982, when the peg to the French franc was discontinued, the exchange rate was managed with reference to a basket of ten currencies. However, by end-1991, the authorities ceased the practice of adjusting the exchange rate to offset inflation differentials with key trading partners. Since May 9, 1994, the Malagasy franc has been allowed to float freely. The exchange rate in terms of the SDR at end-September 2002 was FMG 8,958 = SDR 1.

Madagascar accepted the obligations under Article VIII, Sections 2(*a*), 3 and 4 on September 18, 1996 and maintains no restrictions on the making of payments and transfers for current international transactions.

X. Last Article IV Consultation:

Madagascar is on the standard 12-month Article IV consultation cycle. The 2001 Article IV consultation discussions with Madagascar were conducted in Antananarivo during the period September 3–17, 2001. The staff report was discussed by the Executive Board on December 5, 2001.

XI. Technical Assistance:

Department	Dates	Purposes	Results of Missions
FAD	July-August 1994	Assess the decline in the country's tax effort and recommend measures to mobilize additional revenue.	Elimination of all ad hoc tax exemptions, beginning with the 1995 budget, recommended.
FAD	September 1995	Assess the need for reforming the value-added tax (VAT) and develop a strategy to improve tax and customs administration.	Broadening of the VAT base and the creation of a special office for the monitoring of transactions in the free export zone recommended.
FAD	September 1996	FAD advisor to assist the authorities in implementing the recommendations of FAD September 1995 mission. Assignment extended to March 1998.	The large-taxpayer unit established. Implementation of VAT reform continued.
FAD	December 1997	Review existing tax incentives and prepare action plan to improve the performance of the tax and customs departments.	Program proposed to curtail exemptions and implement an exemption-monitoring scheme.

Department	Dates	Purposes	Results of Missions
FAD	February 1998	Hold follow-up discussion on tax and tax administration reform program.	Schedule for the preparation and implementation of key measures established.
Department	**Dates**	**Purposes**	**Results of Missions**
FAD	March 1998	Examine and assess budgetary expenditures, control, and management.	Comprehensive report prepared for the reform of budget planning, execution procedures, and control systems.
FAD	April 1998	Review important issues to be addressed in the area of customs administration.	Agenda for follow-up mission identified (July 1998).
FAD	June 1998	Conduct follow-up visit on expenditure control.	Action plan, based on the report of the FAD mission of March 1998, established.
FAD	May, September, and December 1998 and April, May, and June 1999	Hold follow-up discussions on tax and tax administration reform.	Assistance for the revision of the VAT law provided, and a VAT reimbursement system introduced for free export zone producers.
FAD	July 1998	Identify measures to strengthen customs administration.	Report prepared on duty assessment and collection procedures, the coordination between the preshipment inspection company and the customs department, the computerization strategy, and organizational issues.
FAD	January 1999	Help implement earlier FAD recommendations on improving public expenditure management.	Aide-mémoire prepared on progress in harmonization of budget and treasury classifications, computerization of treasury offices, implementation of a cash management and financial plan, and implementation of a budget and accounting classification for the decentralized budget.
FAD	June 1999	Strengthen tax audit system of large-taxpayer unit.	Action program developed and agreed with the authorities.
FAD	February-March 2001	Examine and assess budgetary control and	Comprehensive report prepared for the reform of budget

		management.	planning, execution procedures, and control systems.
Department	**Dates**	**Purposes**	**Results of Missions**
MAE	August 1993-99	Assign a bank supervision advisor and assist in the adoption of an interbank foreign exchange market.	Supervisory agency strengthened.
MAE	April-May 1994	Review the modalities for liberalizing the exchange regime and accompanying monetary and credit measures.	Interbank exchange market adopted in May 1994. Central bank base rate and reserve requirements increased.
MAE	May 1995	Review interbank foreign exchange market, develop indirect instruments of monetary management, and reduce banks' excess reserves.	Recommendations adopted during the second half of 1995.
MAE	October-November 1998	Assess the operation of the foreign exchange and treasury bill markets; introduce the euro quotation currency.	Recommendations for treasury bill market adopted in November 1998.
MAE	December 1998	Prepare the change to the euro as pivot currency.	Euro introduced as scheduled.
MAE	May-June 1999	Prepare for introduction of continuous-quotation foreign exchange market, including procedures manual and market rules.	Recommendations made but not implemented.
MAE	October-November 1999	Assess exchange regulations and the implementation of the Basel Core Principles for effective banking supervision.	Recommendations on banking regulation to be adopted.
STA	October 1995	Review money and banking statistics.	Recommendations for data improvements adopted.

Department	Dates	Purposes	Results of Missions
STA	March 2001	Review balance of payments compilation system.	Recommendations for improvements accepted and currently being adopted.
STA	July-August 2001	Review money and banking statistics.	Recommendations for data improvements accepted and are being adopted.

XII. Resident Representative:

Madagascar has had a Fund Resident Representative since September 1989. Mr. Gregory Dahl took up the post as Senior Resident Representative at end-August 2000.

Madagascar: Relations with the World Bank
(As of November 13, 2002)

Partnership in Madagascar's post-crisis recovery

1. With the resolution of the political crisis in July 2002, the World Bank was in a position to accelerate its assistance because suspension of projects had been avoided during the crisis. As an immediate response to the crisis, the World Bank prepared an Interim Country Assistance Strategy (I-CAS), centered around the (i) restructuring of the project portfolio to better align project with post-crisis recovery needs; (ii) preparation of an Emergency Economic Recovery Credit (EERC) in the amount of US$50 million; and (iii) preparation of a Rural Transport Project in the amount of US$80 million. The Bank's interim objective until the end of 2003 is to limit and reverse the impact of the crisis on the poor by supporting the government's reconstruction and recovery program. Particular emphasis is given to (i) supporting a safety net for the poor; (ii) assisting the private sector to restart production; and (iii) ensuring a minimum of public service delivery.

2. The political crisis ended in July, but the social and economic impact is extremely pronounced, especially on a country with a GNP per capita of US$260 (in 2000), one of the poorest in the world even before the current events commenced. The direct negative impact on national income for 2002 is estimated at half a billion dollars. The total economic cost is much larger, taking into account the loss of confidence, foregone direct investments, foregone exports and physical destruction.

3. On July 26, 2002, the new government presented its reconstruction and development program to the 'Friends of Madagascar' conference organized by the United Nations Development Program, the European Commission and the World Bank at the Bank's Paris Office. Representatives of 17 countries and 19 organizations attended the conference. Donors expressed strong support for the economic and social program of the government of Madagascar and underlined the importance of adhering to principles of good governance, promoting development of a strong private sector, and reducing poverty. In addition, participants emphasized the importance of formulating a poverty reduction strategy in an inclusive way. To support these objectives, donors pledged approximately US$2.3 billion over a period of four years.

Bank Group Strategy and lending operations

4. The Bank's portfolio consists of 19 projects with total commitments of around US$816 million, of which about US$338 million was disbursed as of end-September 2002. Of total commitments, 36 percent are in the social sectors, 20 percent in infrastructure, transport, energy and mining, 16 percent in rural development and environment, 10 percent in institutional development, and 18 percent correspond to macro-economic adjustment. In December 2001, before the crisis started, implementation of all projects but one was rated satisfactory.

5. Portfolio implementation during the crisis greatly suffered because: (i) counterpart funds were not available (which is not a new phenomenon but worsened during the crisis);

(ii) procurement of certain goods and works was stopped due to problems within the relevant government agencies; (iii) decision-making authority was unclear; (iv) sector ministries were unable to function; and (v) project activities could not be carried out in certain areas of the country. As a result, by the end of July 2002, the implementation performance of 16 projects out of 19 was rated unsatisfactory, and among them, five projects were unlikely to achieve their development objectives. In addition, two projects: (i) Second Private Sector Development Project and (ii) Multisectoral HIV/AIDS Prevention Project failed to be made effective due to unclear decision-making authority. Five projects – Capacity Building, Energy II, Environment, Social Fund, and Urban Infrastructure – had to have their closing dates extended so as to be able to complete implementation.

6. In response to the end of the political crisis, the World Bank has prepared an Interim Country Assistance Strategy (I-CAS). The I-CAS' objective is to assist the government to mitigate the impact of the crisis on the poor by supporting selected areas of the government's program. Bank instruments used in response to crises include: portfolio restructuring (including a measure which waves the provision of nontax counterpart funds for selected projects until the end of 2003), new lending (including an emergency credit) and policy advice. The mix of these instruments is determined by (i) the Bank's objective of limiting the impact on the poor; and (ii) the activity of other partner organizations in Madagascar. Table 1 outlines the planned instruments by objective.

TABLE 1: GOVERNMENT STRATEGY AND BANK INSTRUMENTS

	Support to Most Vulnerable	*Assisting Private Sector in Recovery*	*Ensuring Minimum of Public Service Delivery*	*Improving Governance and reducing corruption*
Portfolio Restructuring	Child Nutrition, Community Development, Micro-finance	PSD-2, Transport	Health, Education, Rural Development	Second Structural Adjustment Credit
New Lending	Rural Transport $80 million)	EERC ($50 million)		Mining ($30 million)
Policy Advice/ AAA	Rural Development and Poverty, Poverty monitoring w/ partners	Tourism Sector Note, EPZ study	Decentralization Study	Country Procurement Assessment, Country Financial Accountability Assessment

7. As outlined in Table 1, the Bank is planning to support the new government through analytical work and policy dialogue in several areas. Most of the studies had already commenced before the crisis and are now re-orientated to meet urgent information needs. Policy notes have already been produced on recent poverty developments, the economic cost of the crisis and priorities for reconstruction, as well as on short-term policy to strengthen communities. In addition to the ongoing work on poverty monitoring, the Bank plans to continue working on six formal analytical studies which will also feed into the preparation of the PRSP and will be future building blocks for a possible next adjustment operation. The work includes a report on rural development and poverty reduction, a decentralization study, a study on measures to revive the EPZ, a tourism study, a financial management review, and a country procurement review. A report on poverty developments was completed in FY02.

Thus, all of IDA's core economic diagnostic work is expected to be up to date by the end of FY03 with the exception of a public expenditure review and a Country Economic Memorandum which the Bank intends to carry out in FY04 and FY05, respectively. The program of analytical work also provides the basis for a future Poverty Reduction Strategy Credit (PRSC), which is foreseen during the CAS period following this interim CAS.

8. For the period November 2002-June 2003, the interim CAS foresees three new lending operations for a total of about $160 million:

(i) *Emergency Economic Recovery Credit (US$50 million).* To address urgent financing needs for the next 12 months that cannot be provided through the existing Bank portfolio, this credit over US$50 million will help Madagascar re-launch its economy and support the country's most urgent needs;

(ii) *Rural Transport Project ($80 million).* Poverty in Madagascar is closely linked to isolation from markets and social services. The project will help lower the access costs of rural communities to markets, schools, health centers and other economic and social infrastructure; and enhance the mobility of the rural population to improve their quality of life. This project is part of a sector-wide program co-financed by the European Union, the African Development Bank and the Arab Bank for Economic Development in Africa.

(iii) *Mineral Resources Governance Project ($30 million).* Severe governance problems have characterized Madagascar's mining sector for years but the crisis offers the possibility to decisively reduce illegal activities in the sector. The objectives of the Mineral Resources Governance Project are to (i) strengthen transparency and governance in the management of mineral resources, with special emphasis on small-scale and artisanal mining, (ii) support key institutional reforms for the decentralized management of mineral resources; and (iii) promote private investments and value-added in the mining sector.

IMF-World Bank Collaboration in Specific Areas

9. IMF and World Bank staff maintain a close working relationship, especially with respect to (i) completion of the full Poverty Reduction Strategy Paper; (ii) reforms set out at the decision point of the Highly Indebted Poor Countries Initiatives; (iii) analyses and reforms in public financial management; (iv) other governance reforms, including customs; (v) support of the privatization program; and (vi) participation in the integrated framework trade project. Table 2 includes a short description of each of the areas and specific support from the two institutions with respect to policy advice.

TABLE 2: BANK/FUND COLLABORATION

Area	*Description*	*Specialized Advice/ Reforms Supported by Fund*	*Specialized Advice/ Reforms Supported by Bank*
Completion of full PRSP	Together with multi- and bilateral donors, Bank/Fund work provide continuous technical assistance toward completion of full PRSP, planned in 2003	Macroeconomic framework: growth, revenue, expenditure, trade projections	Poverty analysis; rural poverty study; education and health sector work
HIPC completion point reforms	Regular joint Bank/Fund supervision missions; joint preparation of HIPC 'Tacking Poverty-Related Spending' assessment and action plan	Reforms linked to budgetary accounting and controls	Reforms in education, health, rural transport sector
Public financial management	Joint Bank/Fund missions analyzing fiscal management	Tax analysis and reform, strengthening control organs; expenditure management	Expenditure monitoring and analysis, especially in sectors important for poverty reduction
Other governance reforms	New government has embarked on large governance reform agenda; Bank/Fund staff work closely with UNDP/EU/BAfD staffs on assisting development of implementation plans	Customs	Anti-corruption agenda, decentralization, judicial sector reform
Privatization Program	Close joint monitoring of government's large privatization program comprising four major and several dozen smaller public enterprises	All sectors, especially monitoring of privatization receipts of large enterprises (petroleum, telecom)	All sectors. Reforms in petroleum, telecom, and air transport sector are linked to ongoing adjustment program.
Integrated Framework/ Trade Analytical Work	Draft Integrated Framework paper completed beginning 2002; validation workshops to be organized till end-2002	Macro projections for IF framework paper	Sectoral analysis for IF framework paper

10. Areas where the **Fund takes the lead role** relate to policy advice and reforms with respect to (i) overall economic policy advice and targets for macroeconomic targets; (ii) tax policy and administration; (iii) budgetary accounting; (iv) treasury procedures; (v) public sector wage policy; and (vi) monetary management and exchange rate policy. The Bank team actively participates in discussions between the Fund and the government in all these areas, however, especially with respect to the setting of overall macroeconomic targets as well as tax policy. The government has requested a tax policy technical assistance mission from the Fiscal Affairs Department, which is planned for the beginning of 2003.

11. Areas in which the **World Bank takes the lead** are related to specific sector advice in the areas in which the Bank has active lending operations (especially in the social sectors, infrastructure, agriculture and environment) as well as to a number of analytical studies that are currently being completed (see paragraph 7 above): a poverty assessment, a study on the Export Processing Zone, on the tourist sector, a rural development review as well as two important diagnostics for future budget support operations: a Country Procurement Review and a Country Financial Accountability Analysis. The Procurement Review is expected to be completed at the end of 2002, while the Fiduciary Assessment is scheduled to be carried out at the beginning of 2003. The Fiduciary Assessment mission will include IMF staff. Further, the Bank is starting a Public Expenditure Review during which much consultation with the Fund team will take place.

12. **Joint responsibility** for policy advice between the Bank and the Fund concern (i) budgetary procedures, including expenditure execution; (ii) the functioning of internal and external budget control institutions; (iii) reform of customs; (iv) trade policy; and (v) monitoring and continuation of the privatization program. Further, the two institutions jointly support the PRSP process, the HIPC process, and the completion of the Integrated Framework trade initiative (see Table 2 above).

TABLE 3: MADAGASCAR: FINANCIAL RELATIONS WITH THE WORLD BANK GROUP

Statement of active IDA credits (as of November 10, 2002, in millions of original currency)

ID	Project	Orig. Currency	Principal	Avail-able	Dis-bursed	Closing Date
P055166	Community development project	SDR	85.20	74.99	10.21	30-Jun-07
P051922	Rural development support project	SDR	69.20	65.21	3.99	30-Jun-07
P051741	Second health sector support project	SDR	29.00	22.11	6.89	31-Dec-06
P052208	Transport sector reform and rehabilitation	SDR	48.40	32.88	15.52	31-Jul-05
P052186	Micro finance	SDR	12.10	6.82	5.28	31-Dec-04
P062628	Regional development	SDR	3.40	3.08	0.32	31-Dec-04
P001568	Nutrition II	SDR	20.40	6.96	13.44	31-Jan-04
P001564	Rural water sector pilot	SDR	12.60	7.84	4.76	31-Dec-03
P001559	Education sector development	SDR	47.70	31.54	16.16	31-Oct-03
P001533	Energy sector development project	SDR	31.80	6.05	25.75	30-Jun-03
P076245	Mineral resources governance project	US$	0.95	0.86	0.10	15-Mar-03
P040019	Capacity building	SDR	9.60	0.00	9.60	31-Dec-02
P001555	Private sector development and capacity building	SDR	17.20	0.73	16.47	31-Dec-02
P048697	Urban infrastructure	SDR	25.20	13.08	12.12	31-Dec-02
P056487	Mining project	SDR	3.80	0.61	3.19	31-Dec-02
P057378	SAC II	SDR	73.50	0.00	73.50	31-Dec-02
P001537	Environment II	SDR	20.60	0.69	19.91	31-Dec-02
P072987	Multisectoral STI/HIV/AIDS	US$	0.60	0.00	0.60	13-Dec-02

Note: An Emergency Recovery Credit (US$50 million) is in the final stage of preparation.

Madagascar: Statistical Issues

1. Madagascar's database remains weak, particularly as concerns the real sector, government finances, the balance of payments, and social indicators. The authorities are aware of these deficiencies and are working, with technical assistance from the international community, including the Fund, to strengthen their statistical system. Madagascar is taking steps to participate in the General Data Dissemination System (GDDS). To this end a GDDS coordinator has been approved and metadata are under preparation. STA balance of payments and monetary and financial statistics technical assistance missions visited Antananarivo in June and July 2001.

Real sector

2. The introduction in 1996 of a system of regular business surveys has contributed somewhat to an improvement in the compilation of national accounts data. However, data remain weak and incomplete, particularly for the agricultural sector. Data on the use of resources are also inadequate, and data for changes in inventories are not reported. Short-term indicators of economic activity, are not generally available. Significantly, in January 2002, the publication of a quarterly index of industrial production by export processing zone (EPZ) enterprises was introduced, with external technical and financial assistance. There are plans to begin developing a quarterly industrial production index (covering non-EPZ enterprises), should discussions concerning UNDP financial assistance be completed shortly. Plans to revise the national accounts methodology and update national accounts on the basis of the 1995 input-output table have been delayed for several months due to the political crisis.

3. A revamped consumer price index (CPI), with weights based on the1993 household survey and covering four principal cities, was introduced in July 2000. The CPI is generally reported to Fund staff on a timely basis; however, during the period January-August 2002, the compilation of the price index was disrupted and reporting delayed; timely reporting resumed in September. Data on producer prices and nationwide employment are not available.

Government finance

4. The Treasury reports monthly data on a commitment and on a payments order basis a few weeks after the end of the month. These data are based on information on monthly operations, but do not reflect accounting balances, since these are compiled with long delays and in a noncomprehensive manner.

5. The latest government finance statistics (GFS) data reported to STA for publication in the *GFS Yearbook* are for 2000 and cover the consolidated central government. However, detailed information is missing in the time series since 1996 for budgetary and nonbudgetary breakdowns and for central government debt.

Balance of payments

6. Since 1984, the Central Bank of Madagascar (CBM) has been in charge of compiling and disseminating balance of payments statistics, and in 1997 it implemented the fifth edition of the *Balance of Payments Manual (BPM5)*. However, the current compilation system is flawed in many respects: the external trade data are derived from customs data, which are affected by inadequate coverage at the level of recording procedures, and by large amounts of smuggling, particularly in the mining sector. Moreover, the customs processing system has experienced numerous technical disruptions since 1998. As a result, the external trade data have limited serviceability and require many manual corrections. The current implementation of the ASYCUDA (automated system for customs data, version 2.7) was largely completed by mid-2002, with the system installed in most of the customs offices. There are plans to upgrade the customs processing system to ASYCUDA 3++; an UNCTAD technical assistance mission to secure its implementation is expected before end-2002.

7. The accuracy of other balance of payments items is still hindered by inadequate data collection from commercial banks, which continue to use categories and definitions derived from the *BPM4*. These impede the proper classification of reported data. In addition, as the exchange control framework has been eased during the last few years, the collected data cover a shrinking part of the total transactions. As a result, critical balance of payments data (e.g., foreign direct investment, commercial bank assets and liabilities, transportation, construction and other services to enterprises, private transfers) are underreported.

8. Against this background, a balance of payments statistical mission (June 5-20, 2001) reviewed the compilation system within the framework of the *BPM5*. The mission assisted the authorities in integrating customs data in the balance of payments statistics, reviewed the commercial banks data collection system, and drafted surveys to cover nonreported transactions. In addition, the mission instructed the central bank staff on the methodologies outlined in the *BPM5* and provided guidance to the authorities in implementing the GDDS. The mission recommended other measures aimed at improving the existing compilation system, including institutional reforms within the CBM and measures to improve interagency cooperation, which are being implemented.

9. The compilation of external debt statistics is generally satisfactory, and the authorities are benefiting from technical assistance by the United Nations Conference on Trade and Development (UNCTAD) in installing the latest version of the Debt Management and Financial Analysis System (DMFAS). This system should become fully operational by end-2002, follow the completion of data entry, expected to be completed during an October-November UNCTAD mission to Antananarivo.

Monetary statistics

10. Recommendations by the money and banking statistics mission of October 1995 were for the most part implemented, including the reclassification of some accounts of the monetary authorities and commercial banks and the revision of valuation procedures for foreign-currency-denominated accounts. A STA monetary and financial statistics mission visited Antananarivo in July 2001 to follow up on the recommendations of the 1995 mission, assist the staff of the CBM in addressing data collection, compilation, and dissemination issues, initiate work toward introduction of the methodology in the *Monetary and Financial Statistics Manual*, and assist in drafting GDDS metadata for the financial sector. It specifically recommended (1) the widening of statistical coverage to microfinance institutions; (2) the inclusion of the Savings Bank and Postal Administration in the other depository corporations subsector; and (3) the improvement in the timeliness of the BCM's balance sheet. An action plan for the implementation of the mission's recommendations has been agreed with the authorities. Beginning in August 2001, monetary data for publication in *International Financial Statistics (IFS)* have been reported to STA regularly by e-mail. During the 2002 political crisis the timeliness of monetary data reporting has been uneven; however there has been an improvement starting mid-year. Data for the monetary authorities and deposit money banks through August 2002 have been published in *IFS*.

Madagascar: Core Statistical Indicators
(As of November 15, 2002)

	Exchange Rates	International Reserves	Central Bank Balance Sheet	Reserve/ Base money	Broad Money	Interest Rates	Consumer Price Index	Exports/ Imports	Current Account Balance	Overall Government Balance	GDP/ GNP	External Debt/Debt Service
Date of latest observation	11/14/02	09/30/02	09/30/01	09/30/02	09/30/02	11/06/02	09/2002	12/2001	12/2001	08/2002	2001	2001
Date received	11/14/02	10/17/02	10/17/02	10/17/02	10/17/02	11/06/02	10/17/02	10/08/02	10/08/02	11/07/02	10/08/02	10/08/02
Frequency of data	D	M	M	M	M	M	M	A	A	M	A	A
Frequency of reporting	W	M	M	M	M	M	M	V	V	M	V	A
Source of update	A	A	A	A	A	A	A	A	A	A	A	A
Mode of reporting	M	M	M	M	M	M	M	V	V	M	V	V
Confidentiality	C	C	C	C	C	C	C	C	C	C	C	C

Notes: Frequency of data: D=daily; M=monthly; Q=Quarterly; A=annual.
Frequency of reporting: W=weekly; M=monthly; Q=quarterly; A=annually; V=irregularly in conjunction with staff visits.
Source of update: A=direct reporting by the Central Bank of Madagascar, Ministry of Finance and Economics, or other official agency.
Mode of reporting: M=mail (including e-mail); V=staff visits.
Confidentiality: C=unrestricted use.

INTERNATIONAL MONETARY FUND
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EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 03/07
FOR IMMEDIATE RELEASE
January 9, 2003

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

IMF Concludes 2002 Article IV Consultation with Madagascar

On December 23, 2002, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Madagascar.[1]

Background

Since the mid-1990s to end-2001, Madagascar had made significant progress in terms of macroeconomic stabilization and structural reform. Over the period 1997-2001 the growth rate of real GDP averaged 4 ¾ per cent, while inflation remained subdued. Madagascar's balance of payments position strengthened, spurred by foreign direct investment in the export processing zone and growth in nontraditional exports, permitting a significant improvement in the country's international reserves position. Over the same five-year period, the public finances improved and significant progress was made on an ambitious public enterprise and regulatory reform agenda.

Notwithstanding these achievements, poverty remains pervasive despite some recent reductions in urban poverty, and growth prospects constrained by structural impediments and governance-related problems. Moreover, weaknesses in tax administration limit the government's ability to mobilize revenue, leaving Madagascar with limited resources for poverty reduction and dependent on foreign assistance.

Macroeconomic developments in 2001 were encouraging. Real GDP rose by 6 percent, resulting in a further increase in real per capita GDP, and the 12-month rate of inflation was

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. This PIN summarizes the views of the Executive Board as expressed during the December 23, 2002 Executive Board discussion based on the staff report.

reduced significantly, declining from over 8 ½ percent at end-2000 to 4 ¾ percent in December 2001. In 2001, the authorities satisfactorily implemented envisaged reforms in the area of budgetary management, treasury accounting, tax administration, and public enterprise reform. However, fiscal performance in 2001, and particularly over the second half of the year, fell substantially short of target, owing largely to weaknesses in the customs administration.

The political crisis during the first six months of 2002 entailed substantial economic costs. Blockades brought industrial production to a virtual halt and most employees of export processing zone enterprises were laid-off during the first half of the year. The Malagasy authorities estimate that real GDP in 2002 could drop by as much as 12 percent. Inflation, which rose to over 20 percent at the height of the crisis, but which has been declining since June, is projected at 12 percent for end-2002. The crisis has led to a deterioration of the balance of payments and fiscal situations, with revenues and expenditures both down sharply. Income poverty has been estimated to have increased from 69 percent in 2001 to 75 percent in 2002, and the utilization of health services has dropped sharply.

The new Malagasy authorities, starting in July, have moved to ameliorate the situation with the introduction of various temporary tax measures to promote economic recovery and financial support measures designed to alleviate the impact of the crisis on the most vulnerable social groups, including the suspension of user fees for health and educational services. Following a July conference where donors pledged significant assistance, the authorities have been able to clear all of the external payments arrears and a significant proportion of the domestic arrears that had built up during the crisis. The authorities and donors have made the development of infrastucture and the social sectors key priorities, and have accelerated the public investment program beginning at mid-year. Since the reopening of the foreign exchange market in August, the exchange rate of the Malagasy franc has been relatively stable while official reserves have strengthened.

The authorities anticipate an economic recovery next year when real GDP is projected to increase by about 8 percent, led by a pick-up in exports and foreign-financed investment spending.

Executive Board Assessment

Executive Directors noted that following strong performance in 2001, the political crisis of the first half of 2002 had severely affected economic activity. The almost complete shutdown of the export processing sector had increased unemployment, and blockages in the transportation network had impaired the marketing of agricultural output, causing a fall in real income. Directors commended the actions taken by the new government to spur economic recovery through prioritization of expenditures, faster implementation of foreign-financed investment projects, and the adoption of measures to boost confidence and encourage the return of private investors. They also welcomed the measures taken, with donor assistance, to alleviate the increased poverty caused by the crisis and to provide incentives for the poor to utilize the public health and education services. These policies were beginning to re-establish confidence, as seen in the recent upturn in economic activity and tax revenues. In the medium term, the authorities will need to consolidate the progress made in reinvigorating private sector growth and the export processing sector, and in improving the efficiency of the tax system and customs administration. Directors considered it crucial that the authorities work to ensure the optimization of debt relief expected under the enhanced HIPC Initiative, in particular by focusing resources freed through debt relief on measures to improve social conditions and reduce poverty, especially in the rural areas, which had notably not benefited from the broad progress that had been made in poverty alleviation in the 1990s.

Directors welcomed the authorities' determination, as shown by the recent establishment of an anti-corruption commission, to fight corruption and increase transparency, which are essential to stimulate private investment and growth. They also welcomed the steps taken at the government level to implement better control and monitoring mechanisms, as well as the strengthening of the Audit Court, the Directorate-General for Expenditure Commitment Control, and the State Inspectorate-General. Directors urged the authorities to pursue vigorously the ongoing reforms of the judicial system and commercial law.

Directors noted the reduction of customs tariffs on a number of key intermediate products and equipment, aimed at stimulating recovery. In this regard, they underscored the importance of undertaking tax policy changes in a comprehensive framework, accompanied by strengthened tax administration so as to maintain revenues. Directors therefore welcomed the steps taken to strengthen customs administration. A few Directors considered that the reduction in customs duties might have waited until steps were taken to improve enforcement of the tax code. A few other Directors considered that stronger efforts to incorporate the artisanal gem stone mining industry into the formal economy had the potential to raise fiscal revenues.

On the expenditure side, Directors underscored the importance of improving the targeting of pro-poor expenditures, and strengthening budgetary reporting and treasury accounting to ensure that adequate controls on spending are in place. They commended the authorities for their efforts to reduce rapidly domestic arrears. Directors welcomed the authorities' decision to move forward on social and development project execution, which will strengthen social services and increase productivity and incomes especially in rural areas.

Directors agreed with the authorities that monetary policy should be geared to containing inflationary pressures, while ensuring that government borrowing would not pre-empt appropriate levels of credit to the private sector as it recovered from the effects of the 2002 political crisis.

Directors considered that the banking system had weathered the political crisis well, continuing its operations and ensuring the functioning of the payments system. However, they noted with concern the increase in nonperforming loans, as the financial situation of many borrowers had been negatively affected by the crisis. Directors recommended that the quality of bank loans be monitored closely, and that banks increase their loan loss provisioning as needed. They welcomed the measures taken by the bank supervisory agency to monitor the compliance of the banks with the legislation on anti-money laundering and combating the financing of terrorism.

Directors considered the authorities' policy of allowing the exchange rate of the Malagasy franc to float as broadly appropriate, as the excessive appreciation of 2000 and 2001 has been partly reversed and wage rates in particular remain competitive.

Directors drew attention to the burden placed on the national budget of underperforming and inefficient state enterprises, in particular the cotton and sugar companies. They considered that privatization of these and other state enterprises would both remove a drain on the budget and help to spur private sector development and enhance prospects for job creation in the medium term.

Directors regretted that despite the good economic performance in recent years, poverty remains pervasive, and that no appreciable decline in poverty has occurred in rural areas. This called for more intensive and comprehensive efforts to improve productivity in agriculture, diversify the production base, and build rural infrastructure, including roads, schools, and clinics. Directors urged the authorities to effectively monitor outcomes to ensure the development of human capital and investment in infrastructure to support private sector growth. They recommended that the authorities take advantage of the opportunity provided by the PRSP process to prioritize carefully the reform agenda, and to formulate medium-term development plans, including specific poverty reduction programs, in a coherent macroeconomic framework.

Madagascar's statistical database is considered adequate for surveillance and program monitoring. Nonetheless, Directors noted that weaknesses remain in terms of data quality, coverage, and timeliness, and urged the authorities to correct them, where necessary with technical assistance.

Public Information Notices (PINs) are issued, (i) at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies; and (ii) following policy discussions in the Executive Board at the decision of the Board. The Staff Report for the 2002 Article IV Consultation with Madagascar is also available.

Madagascar: Selected Economic Indicators

	1999	2000	2001
	(Annual percent change, unless otherwise indicated)		
National accounts and prices			
Real GDP	4.7	4.8	6.0
Consumer price index (end of period)	14.4	8.7	4.8
Money and credit			
Broad money (M3)	19.5	18.8	16.2
External sector (in terms of SDRs)			
Exports, f.o.b.	11.3	47.6	14.3
Imports, c.i.f.	7.4	45.2	14.6
Current account balance (in percent of GDP)			
Including official transfers	-5.4	-5.7	-1.3
Excluding official transfers	-6.3	-6.5	-2.0
Gross official reserves (in millions of SDRs)	165.5	218.7	317.5
(in weeks of imports of goods and nonfactor services)	9.8	10.2	14.4
	(In percent of GDP)		
Public finances			
Overall government balance			
Including grants	-2.8	-2.8	-4.3
Excluding grants	-6.4	-6.4	-8.1
Tax revenue	11.0	11.3	9.6
Poverty			
National poverty rate (in percent of total population)	71.3	...	69.0

Sources: Malagasy authorities; and IMF staff estimates

INTERNATIONAL MONETARY FUND

NEWS BRIEF

FOR IMMEDIATE RELEASE

News Brief No. 02/133
FOR IMMEDIATE RELEASE
December 23, 2002

International Monetary Fund
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Washington, D. C. 20431 USA

IMF Completes Second Review Under Madagascar's PRGF Arrangement and Approves US$15 Million Disbursement

The Executive Board of the International Monetary Fund (IMF) today completed the second review of Madagascar's performance under an economic program supported by the Poverty Reduction and Growth Facility (PRGF) arrangement. As a result, Madagascar will be able to draw up to SDR 11.347 million (about US$15 million).

The Executive Board extended the arrangement until end-November 2004, given the interruption in the implementation of the PRGF-supported program during the political crisis of early 2002, and waived Madagascar's non-observance of the structural performance criteria on the non-accumulation of external payments arrears in early 2002 and those for end-2001 concerning tax revenue, government domestic financing, and the net domestic assets of the central bank, and the net domestic financing of the government, and on fiscal revenue.

The Executive Board also approved an SDR 2.887 million (about US$4 million) disbursement as additional interim assistance under the enhanced HIPC Initiative for Madagascar for the period January 1, 2003-December 31, 2003.

Madagascar's three-year program was approved on March 1, 2001 (see Press Release No. 01/7), for SDR 79.4 million (about US$106 million). So far, Madagascar has drawn SDR 22.69 (about US$30 million) under the arrangement.

The PRGF is the IMF's concessional facility for low income countries. It is intended that PRGF-supported programs are based on country-owned poverty reduction strategies adopted in a participatory process involving civil society and development partners and articulated in a Poverty Reduction Strategy Paper (PRSP). This is intended to ensure that PRGF-supported programs are consistent with a comprehensive framework for macroeconomic, structural, and social policies to foster growth and reduce poverty. PRGF loans carry an annual interest rate of 0.5 percent and are repayable over 10 years with a 5 ½-year period on principal payments.

After the Executive Board's discussion on Madagascar, Anne Krueger, First Deputy Managing Director and Acting Chair, stated:

"Following a strong economic performance in 2001, the political crisis of the first half of 2002 had severe adverse effects on economic activity, real income, and poverty. The new authorities are to be commended for the decisive actions they have taken since the middle of 2002 to spur economic activity through a careful prioritization of public expenditures, faster implementation of externally funded projects, and adoption of measures to boost confidence and encourage the return of private investors. Inflation has abated in recent months, and economic activity and revenue collection have picked up. External budgetary support has enabled the government to repay a large part of domestic payments arrears built up during the crisis, while external payments arrears were promptly repaid in mid-year.

"The reform package for the rest of 2002 and for 2003 centers on fostering the recovery through continued rapid project implementation, comprehensive reforms in tax and customs administration with a view to widening the revenue base, and a lowering of certain tariffs. A determined effort will also be made to fight corruption and to increase transparency at all levels of government. In 2003, real GDP is expected to grow, after declining significantly in 2002, and inflation will be contained. Fiscal reform will focus on improving expenditure prioritization and strengthening budgetary reporting and treasury accounting. Financial reform will focus on removing impediments to bank lending. The privatization program will contribute to faster growth of key sectors, by attracting additional investment.

"The poverty reduction strategy paper, which will be finalized in the coming months, will be a key instrument in guiding the government's poverty alleviation effort. It will prioritize and estimate costs of action plans for rural development and the social sectors. It will also establish monitoring indicators and should strengthen pro-poor budget planning and expenditure tracking, with a view to enhancing the impact of growth on poverty reduction," Ms. Krueger said.