

## **Djibouti: 2003 Article IV Consultation—Staff Report; and Public Information Notice on the Executive Board Discussion for Djibouti**

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2003 Article IV consultation with Djibouti, the following documents have been released and are included in this package:

- the staff report for the **2003** Article IV consultation, prepared by a staff team of the IMF, following discussions that ended in **September 30, 2003**, with the officials of Djibouti on economic developments and policies. **Based on information available at the time of these discussions, the staff report was completed on December 4, 2003.** The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- a staff statement of **January 7, 2004** updating information on recent developments.
- a Public Information Notice (PIN) summarizing the **views of the Executive Board as expressed during its January 7, 2004 discussion** of the staff report that concluded the Article IV consultation.

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

Selected Issues Paper  
Statistical Appendix

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# INTERNATIONAL MONETARY FUND

## DJIBOUTI

### Staff Report for the 2003 Article IV Consultation

Prepared by the Staff Representatives for the 2003 Consultation with Djibouti

Approved by Sena Eken and Matthew Fisher

December 4, 2003

- The staff team included Messrs. Toujas-Bernaté (head until June 2003), Fasano (head since June 2003), Bessaha, Dridi, and Ms. Touré (all MCD). Mr. Kumah, the IMF resident representative, assisted the February and July 2003 missions.
- Discussions for the 2003 Article IV consultation were held in Djibouti from February 21 to March 7 and July 13 to 20, 2003; with further discussions at headquarters from May 19 to 24, 2003 with Prime Minister Dileita; Economy, Finance, and Planning Minister Bouh; Central Bank Governor Haïd; the ministers of commerce and industry, and employment; other senior officials and representatives of the private sector; bilateral and multilateral donors; and aid agencies. Dialogues with the authorities continued through the resident representative office during the whole month of September 2003 to clarify the 2003 revised budget and in Dubai during the 2003 Annual Meetings. The completion of the discussions was delayed by the late adoption of the 2003 revised budget and the lack, until recently, of a reasonable medium-term macroeconomic framework.
- In concluding the 2001 Article IV consultation in November 2001, Directors noted that growth continued to be weak, reflecting structural rigidities, and that Djibouti's external position remained fragile. On this basis, Directors underlined the importance of steadfast implementation of the fiscal program, including accelerated settlement of budgetary arrears and well-sequenced structural reforms to enhance the economy's responsiveness.
- Against the experience during the last Poverty Reduction and Growth Facility (PRGF) arrangement, the Article IV discussions focused on Djibouti's medium-term outlook and on policies to put the economy on a much higher growth path, which will be critically needed to reduce poverty in the longer term.
- The PRGF arrangement, which was approved by the Executive Board on October 18, 1999, expired on January 17, 2003. As a result of slippages and delays in implementing the program conditionality, only three of six reviews were completed during the arrangement period. The Interim Poverty Reduction Strategy Paper was presented to the Boards of the Fund and the World Bank in November 2001 and a status report on the preparation of the final Poverty Reduction Strategy Paper (PRSP) was presented in December 2002. The authorities plan to present the PRSP to the Boards of the Fund and the World Bank in early 2004. The authorities requested that discussions be initiated on a possible new PRGF arrangement to further support their reform efforts and catalyze external financial and technical assistance.
- The principal authors of the report are Messrs. Toujas-Bernaté, Bessaha, and Dridi.

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## Executive Summary

- **Following six years of adjustment efforts, Djibouti's economic and social situation remains fragile.** Economic growth continues to be constrained by very high production costs and has been insufficient to contribute to job creation and poverty reduction. While the fiscal position was gradually brought under control and progress was achieved in reforming public finance, the structural reform efforts aimed at addressing the constraints to growth were hesitant and modest. As a result, Djibouti still has one of the poorest set of social indicators in the world.
- **Djibouti's short- to medium-term outlook will benefit from increased foreign military stationed in Djibouti, a larger donor-financed public investment program, and a large private project for a new deep water seaport.** The extent to which higher growth would be sustained in the long run and contribute to reducing poverty will depend on accompanying policies. The pace and depth of reforms to support private sector development should increase. The recent establishment of three new public enterprises seems to run against this objective.
- **The large additional revenues derived from the foreign military now stationed in Djibouti should greatly facilitate achieving the fiscal goals** of increasing expenditure for priority sectors and steadily reducing the large stock of budgetary arrears. However, these additional revenues were largely used to increase non-essential expenditures in 2003. The structure of expenditures will need to be significantly altered if the authorities are to succeed in making a dent in poverty.
- **Good progress was achieved in reforming public finance and the legal framework for financial operations, but transparency of public finances could be further enhanced.** Tax administration and expenditure management reforms should be consolidated, work of the public finance auditor's office be made public, and revised banking laws be adopted as soon as possible.
- **Djibouti's external competitiveness will need to be restored to spur lasting economic growth on a sustainable basis.** While the authorities intend to rely only on structural and regulatory reforms to achieve this goal, the staff sees limits in this strategy and takes the view that an adjustment of the exchange rate will be needed.
- **The authorities requested initiation of discussions on a possible new PRGF arrangement.** The staff sees the need for a period of solid policy performance, including by (a) completing growth-enhancing structural reforms that were envisaged under the previous arrangement; (b) adopting a 2004 budget that supports both growth and the poor; (c) orderly settling budgetary arrears; and (d) implementing a carefully thought-through action on the exchange rate supported by the establishment of social safety nets before entering into a new arrangement.

## I. INTRODUCTION AND BACKGROUND

1. **Following six years of adjustment efforts supported by the Fund under Stand-By and PRGF Arrangements, Djibouti's economic and social situation remains fragile.** The fiscal position, which deteriorated markedly in the early 1990s following the outbreak of an ethnic-based conflict, was progressively brought under control and the large stock of domestic budgetary arrears started to decline in 2001. However, economic growth continues to be constrained by very high production costs and has been insufficient to contribute significantly to job creation and poverty reduction. The structural reform efforts aimed at addressing some of those constraints were hesitant and modest. As a result, Djibouti still has one of the poorest set of social indicators in the world. The key policy challenge for Djibouti is to implement a comprehensive strategy to promote private investment and job creation to effectively reduce poverty.

2. **The increased foreign military forces stationed in Djibouti will bring significant additional revenues in the next few years.** These additional revenues should provide much-needed breathing space in fiscal management. The challenge will be, however, to use these resources as efficiently and transparently as possible to support the implementation of the poverty reduction strategy and reduce the large stock of budgetary arrears.

3. **The first multiparty parliamentary elections took place peacefully in January 2003 and were won by the coalition supporting the president.** Nevertheless, the stronger-than-expected result of the opposition signaled the population's concerns regarding the dire economic and financial situation. In outlining the government priorities in the period to the presidential elections in 2005, the prime minister tried to address those concerns and stressed the need for a reduction in youth unemployment, higher economic growth, the pursuit of budgetary discipline, and more government focus on priority social sectors (education, health, and water).

4. **The authorities requested that discussions on a possible new PRGF arrangement be initiated by end-2003.** They see the need for a new arrangement to further support their reform efforts and catalyze continued donors' financial and technical assistance needed for implementing the poverty reduction strategy.

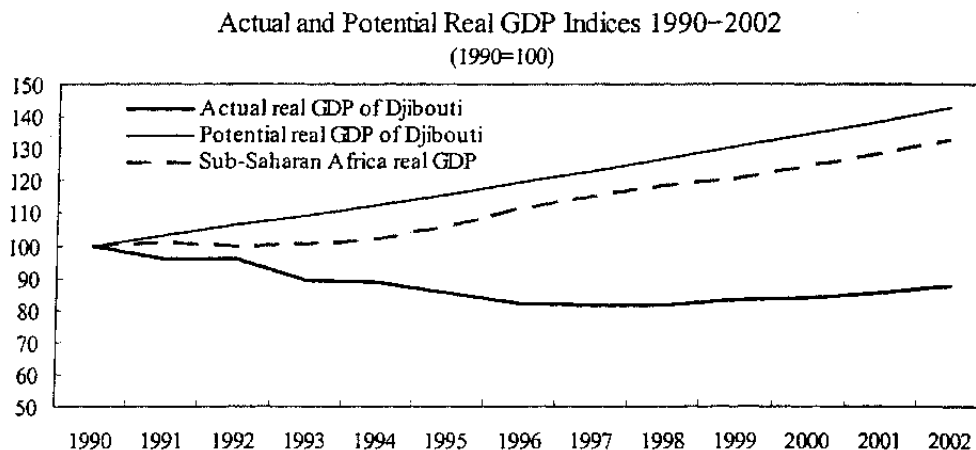
## II. RECENT DEVELOPMENTS

5. **Macroeconomic performance during the program supported by the PRGF arrangement was mixed.** While inflation was reduced as programmed, economic growth was on average only 1.7 percent, much below the 4 percent program objective by the end of the period (Tables 1 and 6). Fiscal discipline was somewhat restored, as evidenced by the curbing of the stock of budgetary arrears. However, the overall fiscal performance lagged well behind the program objectives. Total revenue (as a ratio to GDP) stagnated instead of increasing and the wage bill did not decline as rapidly as expected. Consequently, there was virtually no room for incremental social expenditure and the expected quick reduction in the stock of arrears did not materialize. On the other hand, developments in the external accounts

were more positive (Table 7). The current account deficit was broadly in line with the initial program projections. Moreover, large capital inflows through money changers were recorded toward the end of the program period, which contributed to significant overall balance of payments surpluses. With overall financing requirements turning out to be very close to initial projections, lower program financing from international financial institutions and smaller debt relief were fully offset by larger official grants and net private capital inflows.

6. **The poor economic performance in the last few years contributed to the deepening of poverty.** According to the 2002 household survey, about three-quarters of the population now live in a situation of relative poverty, of which more than half live in extreme poverty.<sup>1</sup> The marked deterioration in poverty indicators in 1996–2002 was accompanied by an increase in unemployment from an estimated 45 to 60 percent. The income distribution remains highly skewed in favor of those able to find employment in the formal sector and is aggravated by the lack of formal safety net mechanisms. Moreover, social indicators in education, health, and access to water remain among the lowest in the world (Table 2).

7. **Economic growth picked up somewhat in 2002 but remained modest.** Real GDP growth was estimated at 2.6 percent in 2002 and is projected at 3.0 percent in 2003—a level that barely stabilized the continued decline of real GDP per capita observed during the last decade and leaving a cumulative output gap with sub-Saharan Africa during the period 1990–2002 of almost 50 percent (Figures 1 and 2). The sectors of commerce, hotels and restaurants, transport and telecommunication benefited from the additional demand for services by foreign military stationed in Djibouti. In addition, the start of a large government project of social housing contributed to a good performance of the construction sector. The port of Djibouti was also able to attract additional transshipment activity owing to security concerns in other ports in the region.



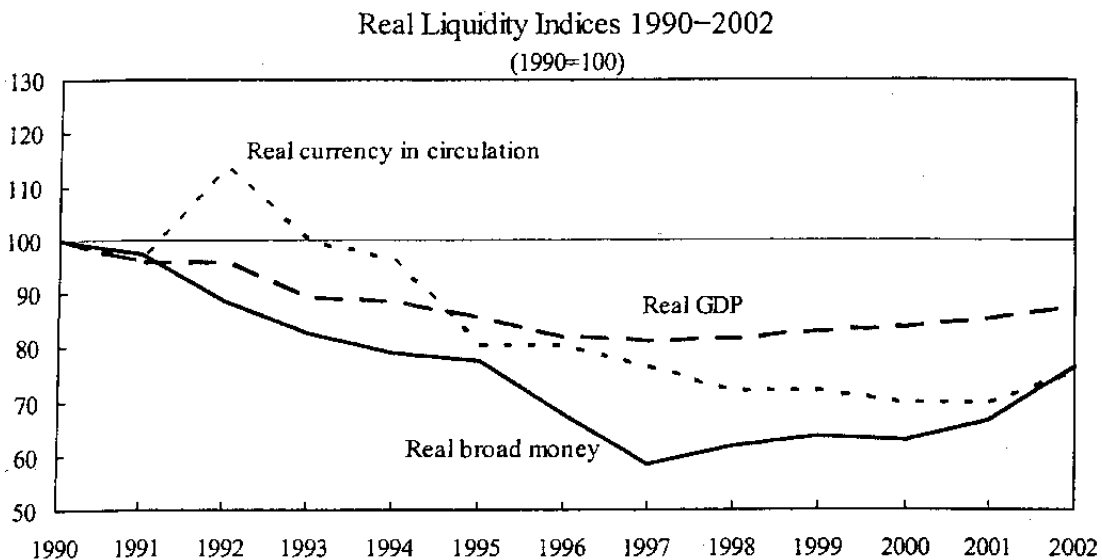
Sources: IMF, *World Economic Outlook*; and staff estimates.

<sup>1</sup> In 1996, less than half of the population lived in relative poverty, with 10 percent living in extreme poverty. In Djibouti, the relative and extreme poverty thresholds, based on relative food consumption and minimum food needs, were estimated at \$3.3 and \$1.8 per capita and per day, respectively.

8. **The fiscal position deteriorated in end 2002 and early 2003, following two years of steady improvement (Table 3).** The domestic fiscal deficit (defined as total revenue minus domestically financed expenditures) increased to 2 percent of GDP in 2002, from 0.3 percent in 2001. Total revenue was lower than expected, mainly because dividends from the port (0.4 percent of GDP) were used off budget to finance security-related expenditures. The wage bill remained higher than budgeted at 14 percent of GDP because of slower implementation of military demobilization and retirement programs. In addition, expenditure in goods and services accelerated markedly during the last quarter in the run-up to the elections, and ended 1.6 percent of GDP higher than expected.

9. **Implementation of the cash treasury plan was abandoned at end-2002 and early 2003, which led to the accumulation of non-wage budgetary arrears.** Fiscal discipline was relaxed under political pressure in the few months preceding and following parliamentary elections. In this context, the bilateral budgetary aid that was disbursed at end-2002, government borrowing from one commercial bank in December 2002, and the additional revenues derived from military cooperation that were disbursed in early 2003 were mostly used to repay wage arrears, while new nonwage arrears external arrears were accumulated. Overall, nevertheless, the stock of domestic budgetary arrears was reduced from 28.9 percent of GDP at end-2001 to 25.3 percent of GDP by mid-2003.

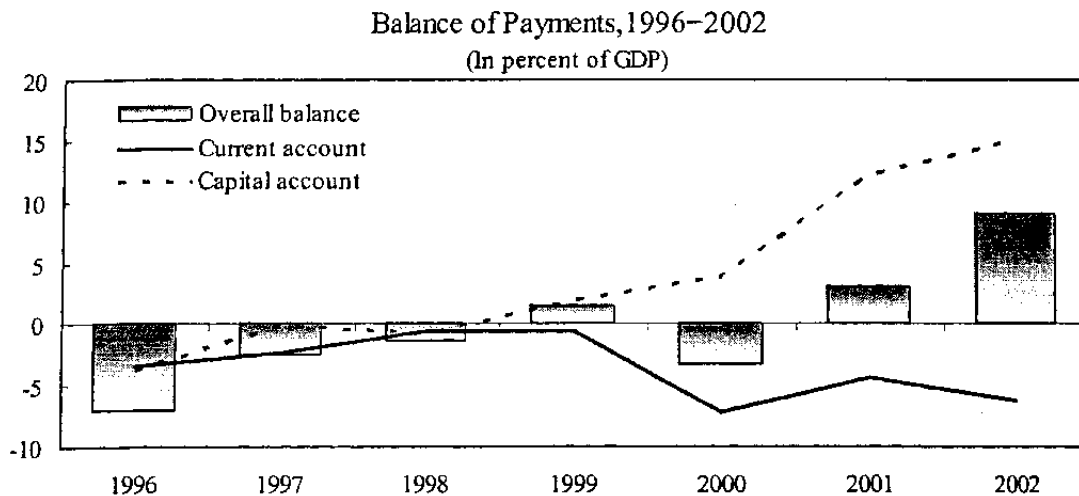
10. **Broad money growth continued to be very strong in 2002 and early 2003, while credit to the private sector declined further (Table 4).** The 20 percent increase in broad money in the year to June 2003 reflects an improvement in the liquidity situation of households following the repayment of wage arrears as well as large (unidentified) capital inflows. At the same time, the decline in credit to the private sector was because of



Sources: Djibouti authorities; and IMF staff estimates.

uncertainties about the economic outlook, the lack of new private sector investment projects, and an upward trend in nonperforming loans.<sup>2</sup> These concomitant developments resulted in a significant buildup in net foreign assets by commercial banks (Figure 3).

11. In the external sector, large capital inflows contributed to an overall balance of payments surplus of about \$55 million (9 percent of GDP) in 2002 (Table 5). The trade deficit widened significantly, reaching 34 percent of GDP, as imports increased because of larger public investment and the presence of foreign military forces. With a surplus in the balance of services, the current account balance recorded a deficit of 6 percent of GDP. This deficit was more than offset by a surplus in the capital account resulting from higher external project financing (all on highly concessional terms or grants) and very large unidentified capital inflows that were channeled through money changers (estimated at about \$50 million).<sup>3</sup>



Sources: Djibouti authorities; and IMF staff estimates.

12. Following the depreciation of the U.S. dollar in effective terms, Djibouti's nominal effective exchange rate depreciated in 2002 and early 2003, but the real effective exchange rate remains highly overvalued. The 16 percent nominal effective exchange rate depreciation of the Djibouti franc<sup>4</sup> between February 2002 and June 2003 was

<sup>2</sup> The share of nonperforming loans increased from 18 to 26 percent between end-2000 and end-2002 (see accompanying selected issues papers).

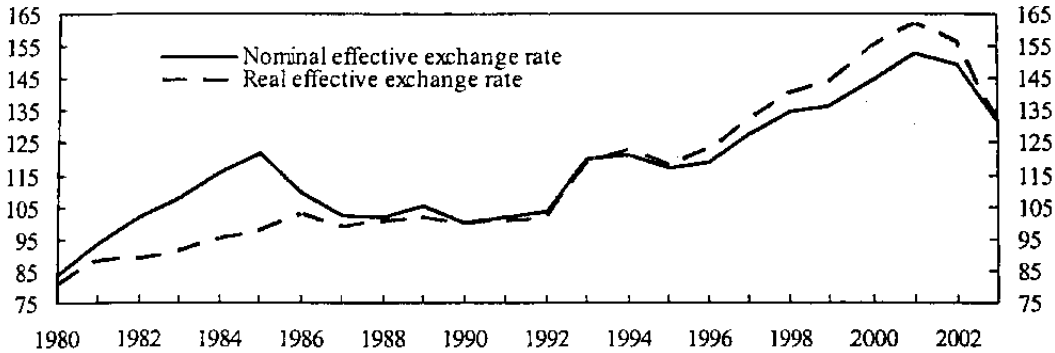
<sup>3</sup> Some of these capital inflows were reportedly linked to the establishment of the U.S. military base in Djibouti.

<sup>4</sup> The Djibouti franc has been pegged to the U.S. dollar at an unchanged parity of 177.7 Djibouti francs per U.S. dollar since 1973.



not sufficient to revert the appreciation in real terms observed in the last two decades. The real effective exchange rate in mid-2003 remained 60 percent more appreciated than in 1980. Such an overvalued exchange rate continues to undermine Djibouti's external competitiveness as argued in the staff analysis that was presented in the 2001 Article IV consultation report (EBS/01/188).<sup>5</sup>

Exchange Rate Developments, 1980–2003 1/  
(1990=100)



Sources: IMF, *Information Notice System*; and staff estimates.

1/ Data for 2003 are up to June only.

13. **The effective exchange rate depreciation was not passed through in higher prices.** The year-on-year increase in the CPI stood at 1.8 percent in June 2003, mainly because of the stability (and in some cases the decline) of prices for several domestic services during the year, including housing, utilities, and transports. At the same time, prices of food items declined slightly.

14. **Many of the structural reforms envisaged in 2002 were not completed even by October 2003.** The revised draft labor code is still under discussion with labor unions, which do not agree with some of its features. The reform of the investment code and the accompanying streamlining and reduction of tax exemptions continue to be debated within the cabinet. Work on the revision of the commerce code started but is proceeding slowly. The financial audits of the remaining main public enterprises (an initial step in the privatization process) were postponed until the second half of 2003 because the accounts of these enterprises for the last couple of years were finalized and certified only in mid-2003.

<sup>5</sup> The staff analysis—while being limited by major statistical weaknesses—reviewed various competitiveness indicators, which provide strong evidence that the real exchange rate of Djibouti has become significantly overvalued.

### III. POLICY DISCUSSIONS

*Against this background and the experience during the last PRGF arrangement, the discussions focused on Djibouti's medium-term outlook and on policies to put the economy on a much higher growth path, which will be critically needed to reduce poverty in the longer term.*

#### A. Experience Under the Last PRGF Arrangement

15. **Important progress was achieved in the last three years in reforming public finance and the legal framework for financial operations.** The following key reforms were implemented during the program period: (a) simplifying the tax structure (income and consumption tax) and improving tax administration; (b) revamping the budget classification and expenditure procedures, together with restructuring the finance ministry to rationalize and streamline budget management; (c) setting up a public finance auditor's office; (d) reforming the pension funds to ensure their lasting financial stability; and (e) establishing a new legal framework to prevent money laundering. In addition, management of the port and airport were privatized, leading to enhanced operations of these enterprises.

16. **Many other structural reforms could not be completed as planned.** None of the reforms aimed at improving the environment for private businesses, such as the reforms of the investment, labor, and commerce codes, could be completed. The demobilization of military personnel hired during the civil conflict was much slower than envisaged and the civil service reform remains at the early stage of planning. Consequently, the still large wage bill has prevented reallocating more resources in favor of priority sectors. Moreover, preparation for the privatization of the electricity, water and telecommunication companies is proceeding very slowly and tariffs on these utilities remain high.

17. **The authorities argued that reform efforts were significant when considering their administrative capacity constraints.** They felt that the program objectives might have been too ambitious in certain areas, not taking enough account of the time needed for building consensus before politically difficult reforms could be implemented. For example, the military demobilization program had to be slowed down following the peace agreement signed with the armed opposition and because of the low level of external financing to accompany this program.<sup>6</sup> The authorities also felt that an overemphasis was placed on fiscal adjustment and reduction in budgetary arrears, while measures benefiting the poor could not be implemented because of insufficient external support. The staff recognized that some of the program objectives were extremely ambitious, including the completion of the reforms of

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<sup>6</sup> In line with the peace agreement, part of the military opposition was integrated into regular military, making it politically difficult to demobilize forces which supported the government during the civil conflict.

the regulatory framework by end-2000 and the elimination of the stock of arrears by end-2002. However, the staff also noted that, while fiscal projections always allowed for additional social expenditures, these objectives were not achieved because measures aimed at making room for such expenditure were not implemented as planned. More generally, reform efforts were slow and often not well coordinated.<sup>7</sup> As a result, many of the commitments under the program could not be fulfilled and only three of six PRGF reviews could be completed during the arrangement period, all of them with a large number of waivers.

## B. Macroeconomic Outlook

18. **The medium-term macroeconomic outlook is dominated by the authorities' plan to launch an ambitious public investment program as a pillar of their strategy to reduce poverty, along with the planned construction of a new deep water seaport.** The latest version of this program, which includes a series of projects aimed at enhancing infrastructure, particularly in the social sectors, would progressively bring public investment from less than 4 percent of GDP in 2002 to more than 8 percent from 2005 onward. The staff warned the authorities of the risks that too ambitious a program could come up against capacity and financing constraints. In addition, for the investment program to be effective and enhance long-term economic growth perspective, it will need to be supported by sound and well-prioritized sectoral strategies. Djibouti's experience in the 1980s showed that large public investment programs did not necessarily lead to sustained economic growth.<sup>8</sup>

19. **Private foreign investors are planning to build a large deep water seaport in Djibouti with an industrial and commercial free zone in the next few years.** This project, estimated to cost about \$400 million (about 60 percent of GDP) over five to seven years and the financing of which is reportedly secured, will include three main phases: a new oil terminal, a container terminal, and an industrial zone. The construction of the new oil terminal started in 2003. The authorities were not yet in a position to make a thorough assessment of the potential impact of this project on growth.<sup>9</sup> They indicated that the regulatory framework under which the industrial zone will operate was still under discussion. In the context of attracting foreign investment, the authorities expected that they would have to grant generous tax exemptions.

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<sup>7</sup> All the attempts at establishing an institutional framework to better monitor and coordinate reform implementation failed, including the latest initiative in late 2002.

<sup>8</sup> In the 1980s, total investment, mainly consisting of public projects, averaged 19 percent of GDP while real GDP growth averaged 2.5 percent.

<sup>9</sup> A large part of the total cost will likely be spent on importing equipment and other inputs for the project, as well as foreign labor.

20. **Assuming that the authorities' public investment program would be implemented as planned, GDP growth would gradually increase over time, but the external debt situation would remain fragile.** In the baseline scenario based on the authorities' policy intentions, and assuming that the public investment program would be fully financed, the staff projects that real GDP growth would increase to about 4 percent by 2006, being mainly driven by the public investment program.<sup>10</sup> The authorities hope to achieve higher economic growth rates than those projected by staff. In the staff's view, given the authorities' cautious and very gradual strategy to restore external competitiveness through structural reforms, private investment, except for the deep water port project, is likely to remain weak. Under these conditions, it is difficult to foresee much stronger growth than projected. The baseline medium-term scenario predicts that the increasing external current account deficit would be financed through higher external public borrowing. As a result, public external debt would increase slightly from 66.5 percent in 2003 to 68.4 percent of GDP in 2005, a level well above the average for sub-Saharan Africa. A debt sustainability analysis indicates that, while external debt would remain sustainable in the baseline scenario, adverse temporary shocks would significantly increase the external debt burden, thus highlighting the need to avoid any macroeconomic slippage and to seek primarily grants or very concessional financing for the public investment program (see Appendix IV).

### **C. Strategy for Enhancing Economic Growth and Reducing Poverty**

21. **The authorities developed a draft Poverty Reduction Strategy Paper (PRSP) through a relatively broad participatory process.** A second round of broad-based consultations was held in July 2003 with participation by elected officials, representatives of the private sector and nongovernment organizations (NGOs), during which the draft PRSP was discussed. Following these consultations, the authorities further revised the PRSP to reflect comments received from the public before sending it to donors for evaluation. The draft PRSP now offers a realistic assessment of the general poverty situation in Djibouti and identifies vulnerable groups that lack access to essential social services.

22. **In the draft PRSP, achieving stronger economic growth and keeping inflation low are underscored as the most effective way of alleviating poverty.** The attainment of the targeted higher growth rates and the reduction in the number of people living in extreme poverty are predicated on the implementation of solid measures to create the conditions for the emergence of new sources of economic growth and to enhance the equity of income distribution. In this context, the staff welcomed the emphasis in the draft PRSP on (a) maintaining macroeconomic and financial stability; (b) reforming the regulatory framework, (c) developing sound micro-finance institutions, and (d) addressing deficiencies in public administration, financial management, and the weak judicial system.

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<sup>10</sup> The authorities intend to organize a roundtable of donors in 2004 to seek full financing for the public investment program.

23. **The staff argued that all the structural reforms will need to be pursued much more forcefully than in the past so as to have their hoped-for effect on economic growth.** In particular, reforms of the investment, labor and commerce codes should be completed expeditiously. Regarding the revision of the investment code, some senior cabinet members are opposed to limiting tax exemptions, which, in their view, remain a powerful tool to attract new investors in Djibouti. The staff noted that experiences in other countries indicate that broad and generous tax exemptions, while clearly eroding the tax base and affecting the buoyancy of the tax system, play a limited role in spurring investment. Ensuring a transparent and efficient level playing field is of much greater importance. In that regard, the staff urged the authorities to make the agency in charge of promoting investment fully operational as soon as possible. The staff also expressed concerns about the recent establishment of three new public enterprises, which clearly run against the government's privatization strategy. The authorities explained that these should be seen as employment-generating programs supporting the poverty reduction strategy.<sup>11</sup>

24. **The draft PRSP supports private sector development as the main engine of growth and underscores the readiness of the authorities to remove obstacles from its development, in particular by improving competitiveness.** The authorities and staff agree that the weak competitiveness of the Djibouti economy, owing to very high labor and other production factors costs, is the main impediment to sustained growth in the future.<sup>12</sup> In the draft PRSP, the authorities are proposing to restore competitiveness through the continuation of structural and regulatory reforms. The staff noted that the proposed strategy for improving the business climate, including the removal of administrative barriers to entry, and for lowering labor and other factor costs remained vague. Moreover, the sectoral strategies and policies to foster diversified growth would need to be better articulated, turned into more operational action plans, and fully costed in the budget framework to ensure their successful implementation. Under the circumstances, the gains expected by the authorities from their reform program in terms of enhanced productivity would not materialize soon, nor be strong enough for achieving the authorities' development objectives. The staff therefore recommended that the authorities should seriously explore other possible policy actions, including an adjustment of the nominal exchange rate, as part of an overall economic policy package to restore external competitiveness and lay the groundwork for sustainable economic growth.

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<sup>11</sup> Establishing the three new public enterprises (mineral water, cement, and stone companies) will cost about 3 percent of GDP and create less than 1,500 new jobs.

<sup>12</sup> The staff analysis of Djibouti's competitiveness that was presented in the 2001 Article IV consultation report remains valid.

25. **The authorities are firmly attached to maintaining the currency board arrangement (CBA) and expressed concerns that a devaluation would have a limited effect on the supply side and might cause serious social and political tensions.** The staff agreed that the CBA has been an important pillar of the fully free exchange and trading systems that Djibouti has maintained for many decades, and contributed to maintaining inflation low. These features should in principle help Djibouti to become a larger regional commercial and financial center. However, rigidities in the labor market and low productivity, coupled with the nominal rigidity inherent in the CBA, have resulted in high output and employment losses. In the staff's view, a devaluation and accompanying reduction in labor cost will eventually be needed to make Djibouti more attractive for investors, facilitate the emergence of new activities in the medium term, and put Djibouti's economic growth on a higher path. It should nevertheless be accompanied by adequate social safety nets in order to mitigate its social impact in the short term. The authorities indicated that they would further consider the appropriate policies to restore competitiveness based on a comprehensive study on how to develop investment and trade currently under way with external assistance.

#### **D. Fiscal Policies and Reforms**

26. **The large additional revenues derived from the foreign military now stationed in Djibouti should greatly facilitate achieving the fiscal goals in the next few years, if used transparently and efficiently.** The authorities and staff agree that the medium-term fiscal framework should aim at the twin objectives of significantly increasing expenditure for priority sectors and, at the same time, steadily reducing the large stock of budgetary arrears. Upon staff's and other donors' insistence, the authorities agreed to the principle of reflecting these additional revenues equivalent to about 4 percent of GDP per year in the budget. Following lengthy discussions and preparation, the authorities finalized and adopted a revised 2003 budget in October, which puts total revenue (excluding grants) at the equivalent of about 27.5 percent of GDP (from 23.5 percent in 2002).

27. **To achieve the medium-term fiscal goals, it will be critical to rein in nonpriority expenditure.** The staff considered it important to follow through on plans announced in the initial 2003 budget to demobilize a large number of military personnel and reduce government consumption of utilities (electricity, telephone, and water).<sup>13</sup> To have a solid basis for additional social expenditure, the staff recommended that the authorities identify detailed measures and programs in priority sectors, the cost of which could be clearly reflected in the budget. They also suggested that military expenditure in goods and services financed with domestic resources could be reduced in view of the large additional external aid in kind that the military are now receiving, and they saw benefits from early repayment of the costly government debt owed to the banking system.

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<sup>13</sup> The initial 2003 budget envisaged the demobilization of 2,000 military personnel.

28. **The revised budget adopted by the authorities increased nonpriority expenditures while leaving modest room for additional social spending.** Among the main changes from the original 2003 budget, the wage bill was increased as a result of a delay and downsizing of the military demobilization program, the integration in the government military of additional members of the armed opposition and the unfreezing of promotion allowances. The budget allocation for utility bills was increased by more than 50 percent, including to cover past bills that were issued late by public utilities. Expenditure in goods and services of the presidency was raised significantly to cover additional travel costs. Finally, the government's share in the newly established public mineral water company was added to public investment. Overall, all these additional expenditure represent about 2.3 percent of GDP. The staff voiced its strong disapproval for such a large increase of what it considers non-essential expenditure, leaving less room for additional spending in priority sectors or repayment of domestic debt. In addition, resources set aside for additional social programs (equivalent to 0.7 percent of GDP) were not applied to detailed actions, and it is not clear how these will be used. Finally, the authorities were not willing to bring forward the repayment schedule on its debt to domestic banks and preferred keeping resources to repay additional wage arrears. The staff expressed the view that for the authorities to demonstrate a strong commitment to their poverty reduction strategy and succeed in attracting donor support, they will need to significantly alter the structure of budget expenditure in favor of priority sectors in the 2004 budget.

29. **The staff urged the authorities to reinstate the treasury cash management plan** which was more or less abandoned at end-2002 and early 2003 following pressures to loosen the budgetary stance in the run-up to the legislative elections. Even with a more comfortable revenue position, the cash plan will help prioritize expenditures and ensure that no new arrears are accumulated. It will also help to maintain the improved coordination between the various directorates of the ministry of finance that this instrument brought about. The authorities agreed with these views and reactivated the cash plan in the second half of 2003.

30. **Resources were allocated in the revised budget to repay domestic arrears, but the overall plan to clear the stock of arrears was not implemented.** Almost no progress was made along the various steps envisaged under the plan.<sup>14</sup> Furthermore, the authorities did not follow the list of priorities for arrears repayment as established in the plan, and repaid only wage arrears while accumulating at times new nonwage arrears. The staff, therefore, called for forceful implementation of the plan to clear domestic arrears.

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<sup>14</sup> These included the following steps: (a) establishing a steering committee to monitor the execution of the plan; (b) publishing a list of creditors with valid claims; (c) providing a legal foundation for the validated claims by issuing adequate instruments; and (d) becoming current on wage payments while securitizing past wages in arrears.

31. **The authorities agreed with staff that to maintain a strong revenue base, they needed to further streamline the tax system, enhance its buoyancy, and modernize tax administration.** Preparations are under way for the reform of business and property taxes, scheduled to be adopted in the 2004 budget.<sup>15</sup> In addition, the staff strongly encouraged the authorities to move speedily on the integration of tax management, control, and collection functions within a single unit. This will further modernize tax administration and pave the way for the introduction of a value-added tax (VAT), scheduled for early 2006. Introduction of a VAT should enhance the buoyancy of the tax system and allow Djibouti to adopt COMESA's common external tariff.<sup>16</sup> In preparation for this reform, the staff encouraged the authorities to accelerate the computerization of customs administration.

32. **The authorities are improving the expenditure control and monitoring framework, but could further enhance transparency of public finance.** Since the year 2000, the government has reformed the entire legal framework governing finance laws and public accounting, as well as the various budgetary, treasury, and accounting procedures. It also reorganized the ministry of finance in late 2002 with a view to streamlining the budget preparation and execution process. However, the authorities have yet to adopt the decrees implementing this reorganization and ensure adequate staffing of key directorates, notably the Budget Directorate. All of these reforms will facilitate budget deconcentration toward line ministries (especially education and health), which in turn should enhance their participation in preparation of the budget and its execution, and ultimately improve their delivery of services. The establishment of the auditor's office in 2000 was another key step in improving transparency of public finance and governance. The staff regretted, however, that the reports prepared by this office on budget execution and public agencies accounts were not made public, and were transmitted only to the president of the republic and the president of the national assembly. The staff also urged the authorities to transfer all government accounts to the central bank and to put the treasurer of the ministry of finance in full control of all those accounts.

### **E. Financial Sector Reforms**

33. **The authorities remain committed to protect the integrity and effectiveness of the banking system.** A new law on money laundering, confiscation, and international cooperation with regard to the proceeds of crime was adopted by the government in

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<sup>15</sup> The reform aims, in particular, at simplifying the depreciation mechanism and introducing more coherence into the schedular direct tax system.

<sup>16</sup> The authorities will need to reform the domestic consumption tax, mostly levied on imports, before introducing new external tariffs.



September 2002.<sup>17</sup> However, the adoption of the revised draft banking law and Central Bank of Djibouti (BCD) statutes, which are being reviewed by the cabinet, was again delayed. The revisions aim at institutionalizing the external audit mechanism of the BCD accounts and remedying remaining weaknesses of the banking laws that were adopted in 2000.

34. **Good progress was achieved in 2002 toward strengthening the BCD's banking supervision capacity.** The BCD completed audits of all the money changers operating in Djibouti in early-2002 and of one of the major commercial banks at end-2002. Looking ahead, the BCD intends to inspect all the banks and the principal money changers once a year. To this end, the BCD launched in end-2002 a program to train its staff with the support of the Bank de France and the Fund, including training for on-site supervision.

35. **The staff welcomed the steps taken by the monetary authorities to regularly audit financial statements of the BCD in accordance with International Standards on Auditing (ISA).** The BCD hired in 2002 new external auditors who audited the BCD accounts for 1999, 2000, and 2001.<sup>18</sup> The final results of this audit are not yet available, but the monetary authorities indicated that preliminary reports from the auditors did not point to any major problem issue. Staff encouraged the authorities to ensure that the remainder of the recommendations of the safeguards assessment report are implemented, including: (a) the publication of the audited financial statements with the audit opinion; (b) the issuance of a management letter; and (c) the modification of the BCD's statutes to reflect new external audit arrangements.

36. **The liquidation of one of the two banks, which were placed under such process in 1998-99, ended, but the pace of the recovery of the assets and reimbursement of depositors of the other bank has been slow.** The authorities indicated that it was mainly owing to judicial delays and difficulties with liquidating assets, mostly in the form of real estate. The staff urged the authorities to conclude the liquidation process of the second bank as soon as possible.

37. **The authorities are developing microfinance institutions which would contribute to the poverty reduction strategy.** The staff stressed that, for these institutions to fulfill their mission and fend off potential political pressure to direct lending to various interest groups, an adequate regulatory environment should be developed so that these institutions are regularly supervised by the BCD. In that regard, the Economic and Social Development Fund

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<sup>17</sup> The authorities also provided answers to the staff questionnaire on "Anti-Money Laundering and Combating the Financing for Terrorism (AML/CFT) Policies and Institutions." The staff, however, did not yet fully assess Djibouti's AML/CFT system.

<sup>18</sup> The same auditing firm will audit the BCD accounts for 2002 and 2003, thus covering a five-year period of audit.

established in early 2003 is not subject to such a supervision by the BCD. Because of this lack of supervision, the staff expressed concern that this Fund might well face difficulties similar to those experienced by the Djibouti Development Bank in the late 1990s that led to its liquidation.

## F. Other Issues

### External debt

38. **Progress has been made in normalizing relations with external creditors, but external arrears remain and bilateral rescheduling agreements are still pending.** The long-standing dispute with France on debt due to Paris public hospitals was settled in June 2002. However, arrears to multilateral creditors remained outstanding until end-December 2002, and new arrears were accumulated in 2003 despite the additional budgetary revenues. Following resumption in late 2002 of the negotiations with member countries of the Paris Club on bilateral debt rescheduling, an agreement was signed with one of the three Paris Club creditors, while the proposals made by the two other creditors were not yet endorsed by Djibouti. One of the agreements not yet concluded is conditional on the full settlement of arrears on nonreschedulable debt. At the same time, the authorities did not actively pursue discussions on rescheduling agreements with non-Paris club creditors. The staff urged the authorities to settle all outstanding external arrears, conclude rescheduling agreements with all Paris Club members, and restart serious negotiations with non-Paris Club creditors.

39. **The authorities launched in 2002 a new project to remedy pervasive weaknesses in external debt management.** As evidenced by errors made in reporting external debt payments at the time of the second review under the PRGF, external debt management has been weak. Recognizing these difficulties, in 2002 the authorities launched a project to improve the database on external debt with financial and technical assistance from the World Bank and the United Nations Conference on Trade and Development (UNCTAD). The new database is expected to be fully operational by end-2003, following a comprehensive inventory of all external loans contracted or guaranteed by the government and completion of training of staff.

### Statistical issues

40. While Djibouti improved its macroeconomic database in recent years, its statistical system continues to fall short of the international standards in terms of quality, frequency, and dissemination. The situation is critical for balance of payments (including trade) and real sector statistics (in particular national accounts). These data weaknesses continue to hamper policy analysis and monitoring. To address these shortcomings, the Djibouti authorities proposed in 2000 a strategy to strengthen Djibouti's statistical system. In this context, the authorities began implementing the recommendations of the various Fund technical assistance missions and merged the national directorate of Statistics with the Central Bureau of Census in 2002 in order to use available staff and financial resources more efficiently.

#### IV. STAFF APPRAISAL

41. **Following several years of financial adjustment efforts, Djibouti's economic growth remains too low to contribute to an effective decline in poverty.** Recent modest real GDP growth is barely stabilizing the continued decline in per capita income observed in the last decade. The poverty and social situation remains extremely severe, with very high unemployment and large vulnerable groups of the population lacking access to essential social services. The economy remains highly dependent on the Djibouti port and its associated activities as well as on the foreign military presence. Against this background, it will be essential to design a credible and comprehensive strategy to create an environment conducive to private investment and increased job opportunities.

42. **Macroeconomic performance and progress in implementing reforms during the last arrangement under the PRGF were mixed.** Fiscal discipline was restored to some extent but fiscal performance lagged well behind the program objectives. As a result, there was very limited room for incremental social expenditures. Concerted efforts resulted in improved tax structure and administration, streamlined budget management, greater transparency in public finances, the adoption of pension reform, and a strengthened legal framework for financial operations. However, work on reforming the investment, labor and commerce codes, and the privatization process could not proceed as initially envisaged. The numerous slippages in policy implementation during the program supported by the PRGF, as well as recent measures such as the establishment of three new public enterprises, raise concerns regarding the level of ownership of the reforms by the authorities.

43. **Djibouti's short- to medium-term macroeconomic performance will benefit from increased foreign military stationed in the country, a larger public investment program and the large private project for a new deep water sea port.** These factors should bring economic growth above the levels experienced in the past few years. The extent to which higher growth would be sustained in the long run and contribute to reducing poverty, including through higher employment, will depend on accompanying policies. In addition, the authorities should be cautious and avoid increasing the already high external public debt burden by seeking primarily grant or very concessional financing for the public investment program.

44. **The pace and depth of reforms should increase to support private sector development, including by improving competitiveness.** The authorities recognize that improvements in competitiveness will be critical to put economic growth on a higher and sustained path. To achieve this objective, the government's strategy aims at broad-based structural reforms and maintenance of financial stability. This strategy should be implemented much more forcefully and coherently than in the past if it has a chance to succeed. However, the staff believes that, even with success, the gains expected by the authorities from their reform program in terms of enhanced productivity would not materialize soon enough and with sufficient strength for achieving the authorities' development objectives. In the staff's view, Djibouti's currency board arrangement represents

a strong constraint for restoring external competitiveness, and an action on the exchange rate should also be part of an overall policy package.

45. **The large additional revenue from the foreign military now stationed in Djibouti should make ample room for additional social expenditures and repayment of domestic debt.** To that end, non-priority expenditures should be limited. The staff strongly regrets the very large increase in nonessential expenditures in the revised 2003 budget, which does not signal a very strong commitment by the authorities to their poverty reduction strategy. If the authorities are to succeed in attracting donor support and make a dent in poverty, they will need to significantly alter expenditures in favor of priority sectors. The military demobilization program should proceed to allow a decline in the wage bill; usage of utilities should be much better controlled; and non-essential expenditures in goods and services should be reduced. In addition, special efforts should be made to identify well-targeted additional expenditures in priority sectors.

46. **The plan to clear the stock of audited domestic budgetary arrears that was prepared by the Ministry of Finance at end-2002 should be made public and implemented decisively.** Repaying the arrears equitably and according to transparent priorities will greatly contribute to restoring the government's financial credibility. The authorities should also seriously consider early repayment of the government's costly debt to the domestic banking system.

47. **The staff commends the authorities for the progress made in modernizing tax administration.** All the measures implemented in this area bode well for preparing the tax administration to be able to introduce and manage a value-added tax in early 2006 as currently planned. However, to do this, it will be essential to further reorganize tax administration to integrate without further delay the functions of tax management, control, and collection.

48. **The staff welcomes the measures taken in 2002 to strengthen the expenditure management process, and encourages the authorities to further enhance transparency of public finances.** The new organization of the finance ministry, which simplifies budget preparation, execution, and control, should be made fully effective with adequate staffing and procedures. The staff recommends that the reports of the public finance auditor's office be made public, and that all government accounts be brought under the direct control of the ministry of finance's treasurer.

49. **The adoption of an anti-money laundering law and the beginning of an external audit of central bank accounts were encouraging steps in protecting the integrity of Djibouti's financial system.** This should be complemented as soon as possible by the adoption of the revised banking law and central bank statutes, as well as by strengthening banking supervision capacity of the central bank and more frequent inspections of financial institutions.

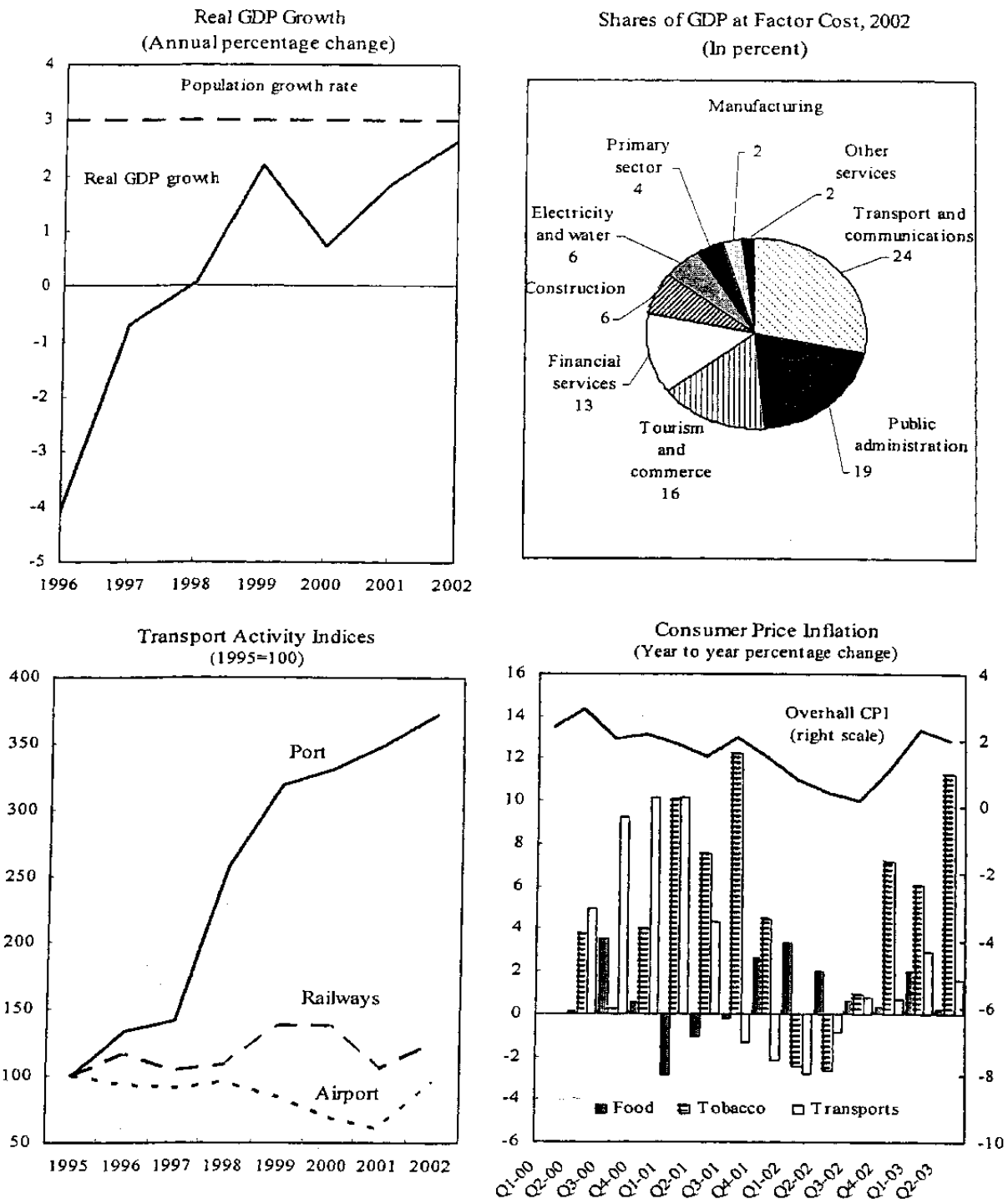
50. **The authorities should fully normalize their relations with donors and settle all remaining external arrears.** This will ensure more steady flows of external resources in support of Djibouti's reform efforts. Renewed efforts should be made to sign rescheduling agreements with Paris Club and other bilateral creditors as soon as possible. The staff welcomes significant improvements in the external debt database. Better external debt monitoring should help avoid any new accumulation of external arrears.

51. **The statistical system should be significantly improved.** Current data weaknesses continue to hamper policy analysis and monitoring. The staff encourages the authorities to strongly implement recommendations of the various Fund technical assistance missions.

52. **The staff sees the need for decisive policy implementation before entering into a new PRGF arrangement.** While the Fund could play a constructive role in the context of a successor PRGF arrangement in spurring reforms and catalyzing external support, the authorities will need to demonstrate a clear, decisive, and broad-based commitment to reform. Therefore, a period of solid policy performance, including by completing many of the reforms envisaged during the last PRGF arrangement, will be required before a successor PRGF arrangement could be considered. In particular, the staff would see the adoption of a 2004 budget that supports both growth and the poor, the implementation of growth-enhancing structural reforms, and the orderly settlement of budgetary arrears as preconditions to enter into a new PRGF arrangement. In addition, in view of the deep-seated competitiveness problems, a carefully thought-through but decisive action on the exchange rate, buttressed by measures to contain the pass-through to wages and establish social safety nets, and supported by prudent fiscal policies, would be needed upfront.

53. It is expected that the next Article IV consultation will take place on the standard 12-month cycle.

Figure 1. Djibouti: Activity and Price Developments, 1996–2002

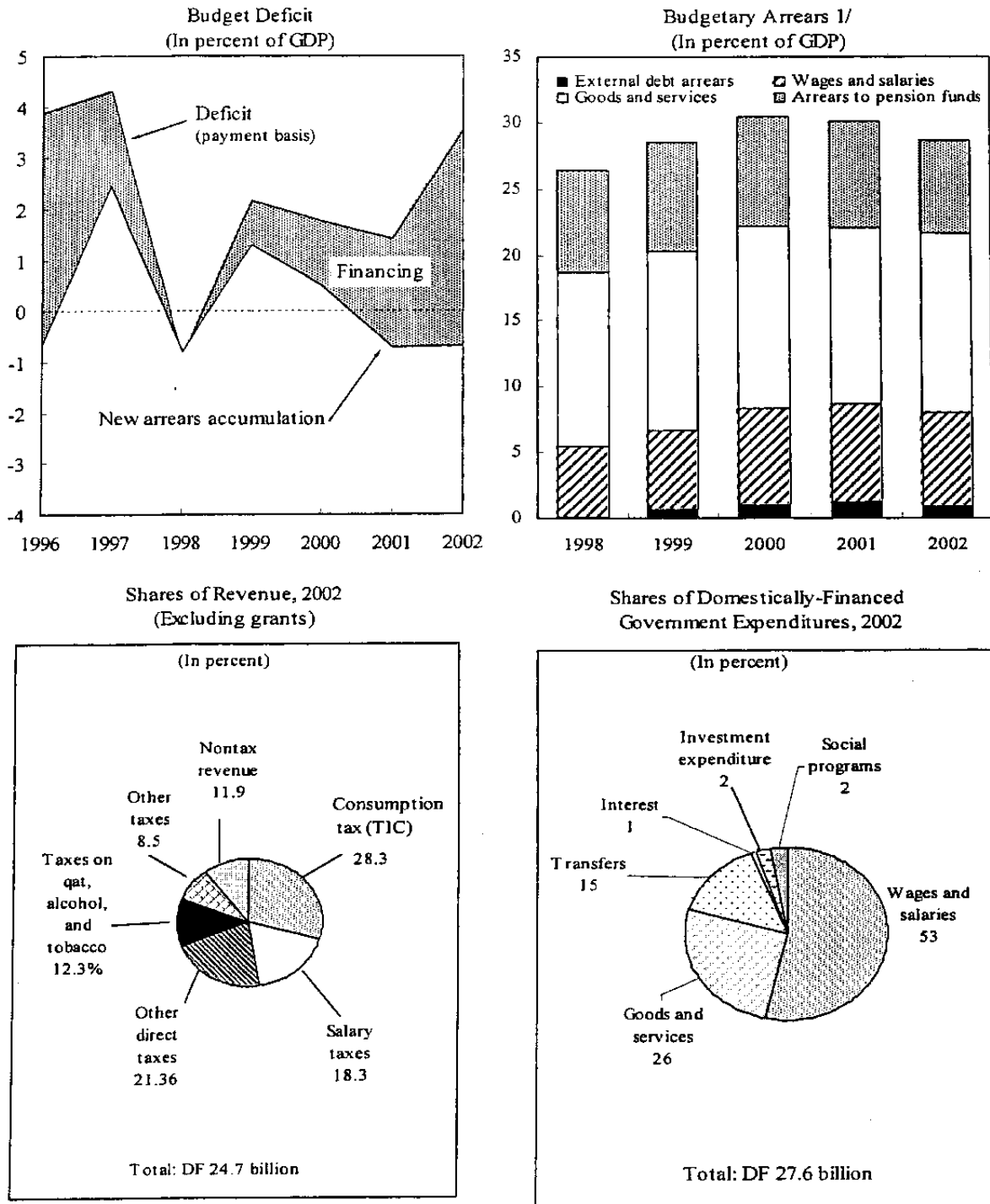


Sources: Data provided by the Djibouti authorities; and IMF staff estimates and projections.

1/ Five-bank basis from 1995 to 1997. Three banks thereafter.

2/ Including errors and omissions.

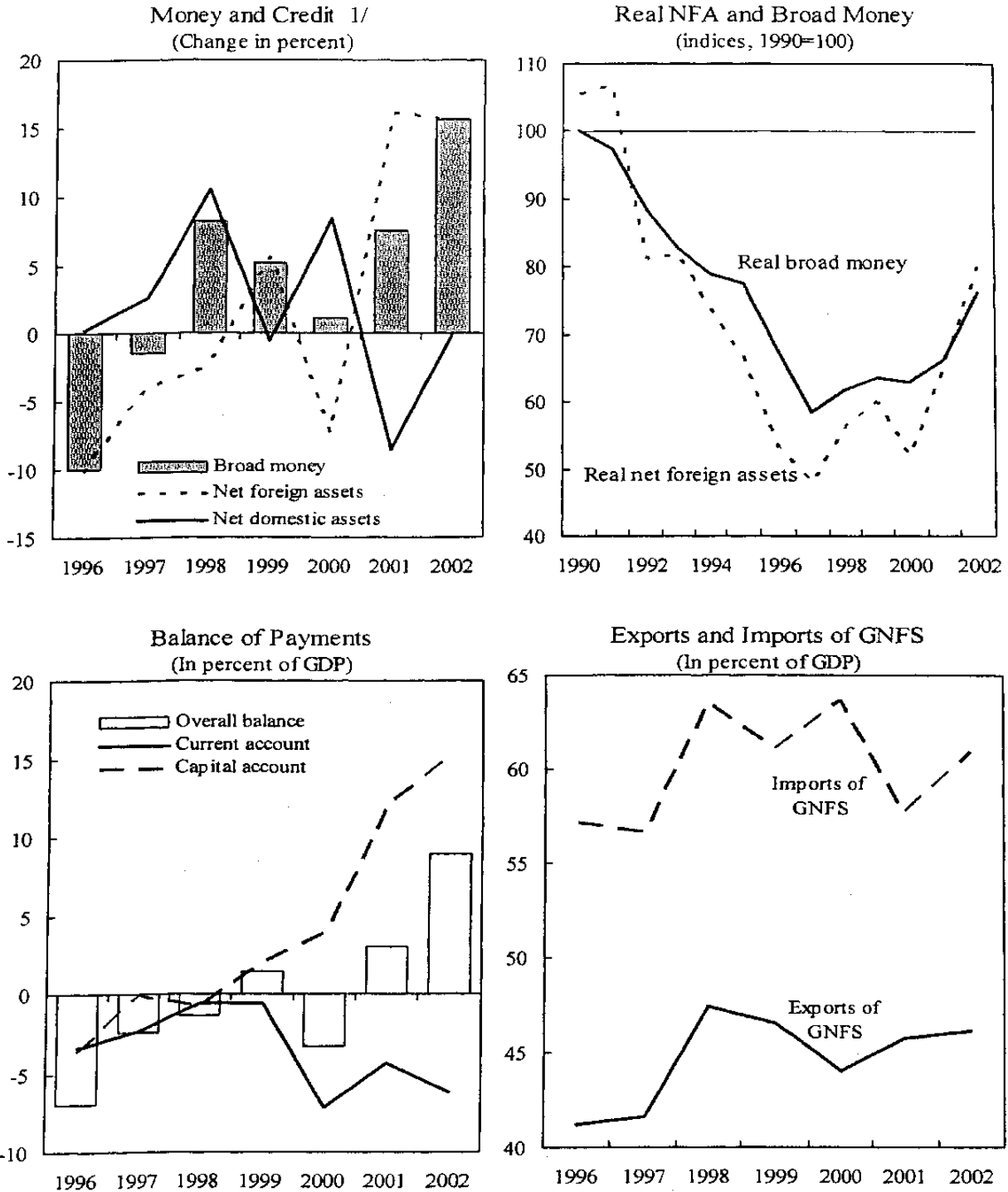
Figure 2. Djibouti: Fiscal Indicators, 1996–2002



Sources: Data provided by the Djibouti authorities; and IMF staff estimates and projections.

1/ To public and private enterprises.

Figure 3. Djibouti: Monetary and External Sector, 1990–2002



Sources: Data provided by the Djibouti authorities; and IMF staff estimates and projections.

1/ Five-bank basis from 1995 to 1997. Three banks thereafter.



Table 1. Djibouti: Selected Economic and Financial Indicators, 1999–2006

	1999	2000	2001	Est. 2002	2003	2004	Proj. 2004	2005	2006
<b>National income and prices</b>									
Nominal GDP (in millions of Djibouti francs)	95,273	98,267	101,870	105,210	110,539		116,264	122,431	129,766
Real GDP (annual change in percent)	2.2	0.7	1.9	2.6	3.0	3.1	3.1	3.2	3.9
Consumer prices (annual average) 1/	2.0	2.4	1.8	0.6	2.0	2.0	2.0	2.0	2.0
(In percent of GDP)									
<b>Investment and Saving</b>									
Investment	8.8	12.2	8.3	10.2	11.8	11.8	20.1	21.0	20.5
Saving									
Domestic saving	-5.7	-7.4	-3.7	-4.6	-6.9	4.3	-4.8	-4.3	-2.3
National Saving	8.2	5.1	3.9	4.0	6.5	7.4	7.1	8.6	9.4
<b>Consolidated government operations</b>									
Total revenue and grants	30.9	31.0	28.2	29.4	34.5	31.2	33.7	33.4	31.5
Total expenditures	33.1	32.8	29.7	32.9	35.6	32.0	36.3	36.4	34.7
Overall balance (payment order basis)	-2.2	-1.8	-1.4	-3.5	-1.0	-0.9	-2.5	-3.1	-3.2
Change in arrears (decrease -)	1.3	0.5	-0.6	-0.7	-2.9	0.0	-2.4	-2.0	-1.9
Overall balance (cash basis)	-0.8	-1.3	-2.0	-4.2	-3.9	-0.9	-4.9	-5.1	-5.1
Government domestic arrears (stock) 2/	29.3	29.6	28.9	27.8	24.9	24.9	22.5	20.5	18.5
(Change from preceding December; in percent of broad money) 3/									
<b>Money and credit</b>									
Broad money	5.2	1.1	7.5	15.7	5.1	5.2	5.2	5.3	6.0
Net foreign assets	5.7	-7.3	16.1	15.7	3.9	2.1	5.1	5.2	5.7
Net domestic assets	-0.5	8.4	-8.6	0.0	1.2	3.0	0.1	0.1	0.3
<i>Of which</i>									
Claims on the central government (net)	-0.2	1.2	1.1	2.8	1.2	0.0	-0.5	-0.6	-0.8
Claims on nongovernment sector	2.7	5.2	-8.2	-2.9	0.0	2.9	0.6	0.7	1.1
(In millions of U.S. dollars; unless otherwise indicated)									
<b>External sector</b>									
Current account	-1.9	-39.7	-24.9	-36.5	-33.0	-30.8	-85.1	-85.5	-81.1
Current account (in percent of GDP)	-0.6	-7.2	-4.3	-6.2	-5.3	-8.1	-13.0	-12.4	-11.1
Trade balance	-182.4	-194.8	-178.7	-200.5	-239.3	-281.9	-281.9	-296.7	-297.3
Transfers (net)	62.7	53.1	31.1	40.6	48.6	-25.8	47.6	51.4	46.0
Capital account	-1.2	30.7	10.2	34.9	43.5	-24.8	79.4	89.8	92.7
Overall balance	7.9	-18.1	39.9	53.0	8.1	-21.8	19.7	21.1	24.2
Official external debt after rescheduling (in percent of GDP) 4/	62.8	66.9	65.2	66.8	66.5	68.0	68.0	68.4	68.3
<b>Debt service ratio</b>									
To exports of goods and services 5/ Obligations basis after rescheduling	8.2	7.3	7.3	7.3	7.7	0.0	7.3	7.2	7.2
<b>Memorandum items:</b>									
<b>Currency board gross foreign assets</b>									
Monetary and LOLR cover (in percent)	111.7	114.9	115.8	114.9	114.2	112.9	112.9	113.0	110.5
As a ratio to currency issue	1.3	1.2	1.2	1.3	1.2	1.2	1.2	1.2	1.2
<b>Exchange rate</b>									
Exchange rate (DF/US\$) end-of-period	177.7	177.7	177.7	177.7	177.7	...	...	...	...
Real effective exchange rate 6/ (End-year change in percent; depreciation -)	6.7	9.3	3.3	-8.4	-10.7	...	...	...	...

Sources: Djibouti authorities; and IMF staff estimates and projections.

1/ Starting in 1999 actual data and projections for 2003 are based on the official CPI introduced in April 1999.

2/ Domestic arrears data include wage arrears, arrears to private and public suppliers for goods and services, and arrears to the pension funds.

3/ Beginning in 1998, data include only three operating banks and exclude two closed banks which are being liquidated.

4/ Public and publicly guaranteed debt of the central government and the public enterprise sector. Data reflect the bilateral debt cancellation agreement signed in 1999, the terms of reference agreed between the members of the Paris Club and the Djibouti authorities for the period 2000–02, and the terms of reference agreed between the Saudi Development Fund and the Djibouti authorities for the period 2001–06.

5/ Exports of locally produced goods and nonfactor services.

6/ Data available through June 2003.

Table 2. Djibouti: Social and Demographic Indicators

<b>Area</b> (thousand sq. km)	23	<b>Population characteristics (2002)</b>	
<b>Poverty and inequality (2002)</b>		Total population	700,000
Percent of expenditure		Annual rate of growth (percent)	2.6
Highest 20 percent	47	Population density (per sq. km)	30.4
Lowest 20 percent	6	Urban population (percent of total)	85
		<b>Health</b>	
Gini coefficient	0.41	Life expectancy at birth (years)	49
Percent of the populations below the poverty line 1/	42	Infant mortality (per 1,000 live births)	103
Rural poverty (percent of rural population)	83	Under five mortality (per 1,000)	124
<b>Labor force (2002)</b>		Child immunization rate (under 12 months)	45
Total participation rate	55	Child malnutrition (2002) (under five years)	43
Unemployment rate	60	Percent underweight	
<b>Education (2002)</b>		Percent stunted	
Gross enrollment rates		HIV/AIDS prevalence rate	2.9
Primary	52	<b>Access to safe water (2002)</b>	
Secondary	32	Percent of total population	84
Teritary		Urban population	93
Illiteracy (percent of adult population)	72	Rural population	52

Sources: Djibouti authorities.

1/ The extreme poverty line, based on minimum consumption food needs, is estimated in 2002 at \$1.8 per capita and per day.

Table 3. Djibouti: Central Government Fiscal Operations, 1999–2006

	Act.		2001	Est.	Rev. Proj.			
	1999	2000		2002	2003	2004	2005	2006
(In millions of Djibouti francs)								
Revenues and grants	29,429	30,467	28,774	30,947	38,183	39,186	40,866	40,901
Total revenue	22,362	23,969	23,702	24,720	30,566	31,764	32,770	33,783
Fiscal revenue	20,605	21,099	20,862	22,164	25,208	26,064	26,733	27,467
Direct taxes	8,469	8,780	9,248	9,804	10,425	10,709	10,910	11,138
Indirect taxes	12,136	12,319	11,614	12,360	14,783	15,355	15,823	16,329
Non tax receipts	1,757	2,870	2,840	2,556	5,358	5,701	6,037	6,316
Official grants	7,067	6,498	5,072	6,227	7,617	7,422	8,096	7,118
<i>Of which</i>								
Fungible aid	1,090	1,020	876	1,042	906	170	170	170
Total expenditure	31,490	32,204	30,215	34,660	39,314	42,148	44,612	44,996
Current expenditure	28,575	29,564	27,688	30,740	34,509	33,848	34,212	34,496
Wages and salaries 1/	14,694	14,609	14,804	14,721	15,364	14,966	14,952	14,911
Materials	6,463	5,991	4,709	6,544	7,578	7,299	6,544	6,388
Maintenance	365	715	515	606	650	683	709	749
Transfers	3,195	3,762	3,533	4,080	4,353	4,141	4,109	4,022
Interest	499	463	301	239	609	558	552	528
Foreign-financed development programs	3,179	4,024	3,826	3,774	5,018	4,035	3,920	3,528
Recurrent charges	0	0	0	0	170	317	612	727
Incremental social programs	0	0	0	775	767	1,849	2,814	3,644
Investment expenditure	2,915	2,640	2,527	3,920	4,805	8,300	10,400	10,500
Domestically financed	399	531	709	596	1,857	600	600	700
Foreign-financed	2,516	2,109	1,818	3,324	2,948	5,900	7,500	7,300
<i>Of which</i>								
Financing to be identified					0	1,800	2,300	2,500
Overall balance (payment-order basis, including grants)	-2,061	-1,737	-1,441	-3,713	-1,131	-2,962	-3,747	-4,095
Change in arrears (cash payments = -)	1,272	466	-605	-717	-3,215	-2,789	-2,500	-2,500
Domestic arrears	1,482	308	-631	-658	-3,215	-2,789	-2,500	-2,500
External arrears on interest and other payments	-210	-184	-25	-37	0	0	0	0
Debt relief on interest payments 2/	0	342	51	-23	0	0	0	0
Overall balance (cash basis)	-789	-1,271	-2,046	-4,430	-4,346	-5,751	-6,247	-6,595
Financing	789	1,271	2,046	4,430	4,346	5,751	6,247	6,595
Domestic financing	320	645	598	1,578	769	-342	-445	-577
Bank financing	278	645	598	1,578	769	-342	-445	-577
Central bank	798	602	579	146	1,064	-47	-150	-282
Commercial banks	-520	43	19	1,432	-295	-295	-295	-295
Nonbank financing	42	0	0	0	0	0	0	0
Securitization of domestic arrears	...	...	0	0	0	0	0	0
Cash repayments of domestic debt	...	...	0	0	0	0	0	0
External financing	469	626	1,447	2,829	3,578	3,592	3,691	3,972
Net borrowing	469	626	1,447	2,829	3,578	3,592	3,691	3,972

Table 3. Djibouti: Central Government Fiscal Operations, 1999–2006 (continued)

	Act.		2001	Est.	Rev. Proj.			
	1999	2000		2002	2003	2004	2005	2006
(In millions of Djibouti francs)								
Disbursements	845	1,015	1,808	3,494	4,280	4,200	4,300	4,600
<i>Of which</i>								
Budgetary aid	0	0	0	1,221	1,209	0	0	0
Amortization payments	-376	-389	-361	-665	-702	-608	-609	-628
Amortization obligations	-592	-671	-526	-470	-685	-608	-609	-628
Change in overdue obligations 3/	216	170	127	-408	-307	0	0	0
Change in nonoverdue obligations	-1,800	-1,800	-1,800	0	0	0	0	0
Debt relief on principal payments 2/	1,800	1,912	1,838	213	290	0	0	0
Residual/financing gap	0	0	0	0	0	2,500	3,000	3,200
Memorandum items:								
Overall balance before grants (payment-order basis)	-9,128	-8,235	-6,513	-9,940	-8,748	-10,384	-11,842	-11,213
Overall balance before grants (cash basis)	-7,856	-7,769	-7,118	-10,657	-11,963	-13,173	-14,342	-13,713
Domestic balance 4/	-2,474	-1,569	-301	-2,128	1,206	3,299	3,409	3,675
Revenue	22,362	23,969	23,702	24,720	30,566	31,764	32,770	33,783
Domestically-financed expenditures	24,836	25,538	24,003	26,848	29,360	28,466	29,361	30,107
Wages and salaries, excluding cost of military demobilization	14,605	14,436	14,596	14,367	15,063	14,852	14,839	14,798
(In percent of GDP)								
Revenues and grants	30.9	31.0	28.2	29.4	34.5	33.7	33.4	31.5
Total revenue	23.5	24.4	23.3	23.5	27.7	27.3	26.8	26.0
Fiscal revenue	21.6	21.5	20.5	21.1	22.8	22.4	21.8	21.2
Direct taxes	8.9	8.9	9.1	9.3	9.4	9.2	8.9	8.6
Indirect taxes	12.7	12.5	11.4	11.7	13.4	13.2	12.9	12.6
Non tax receipts	1.8	2.9	2.8	2.4	4.8	4.9	4.9	4.9
Official grants	7.4	6.6	5.0	5.9	6.9	6.4	6.6	5.5
Total expenditure	33.1	32.8	29.7	32.9	35.6	36.3	36.4	34.7
Current expenditure	30.0	30.1	27.2	29.2	31.2	29.1	27.9	26.6
Wages and salaries 1/	15.4	14.9	14.5	14.0	13.9	12.9	12.2	11.5
Materials	6.8	6.1	4.6	6.2	6.9	6.3	5.3	4.9
Maintenance	0.4	0.7	0.5	0.6	0.6	0.6	0.6	0.6
Transfers	3.4	3.8	3.5	3.9	3.9	3.6	3.4	3.1
Interest	0.5	0.5	0.3	0.2	0.6	0.5	0.5	0.4
Foreign-financed development	3.3	4.1	3.8	3.6	4.5	3.5	3.2	2.7
Recurrent charges	0.0	0.0	0.0	0.0	0.2	0.3	0.5	0.6
Incremental social programs	0.0	0.0	0.0	0.7	0.7	1.6	2.3	2.8
Investment expenditure	3.1	2.7	2.5	3.7	4.3	7.1	8.5	8.1
Domestically-financed	0.4	0.5	0.7	0.6	1.7	0.5	0.5	0.5
Foreign-financed	2.6	2.1	1.8	3.2	2.7	5.1	6.1	5.6
<i>Of which</i>								
Financing to be identified					0.0	1.5	1.9	1.9
Overall balance (payment-order basis, including grants)	-2.2	-1.8	-1.4	-3.5	-1.0	-2.5	-3.1	-3.2

Table 3. Djibouti: Central Government Fiscal Operations, 1999–2006 (concluded)

	Act.		2001	Est.	2003	Rev. Proj.		2006
	1999	2000		2002		2004	2005	
Change in arrears (cash payments = -)	1.3	0.5	-0.6	-0.7	-2.9	-2.4	-2.0	-1.9
Domestic arrears	1.6	0.3	-0.6	-0.6	-2.9	-2.4	-2.0	-1.9
External arrears on interest payments	-0.2	-0.2	0.0	0.0	0.0	0.0	0.0	0.0
Debt relief on interest payments 2/	0.0	0.3	0.1	0.0	0.0	0.0	0.0	0.0
Overall balance (cash basis)	-0.8	-1.3	-2.0	-4.2	-3.9	-4.9	-5.1	-5.1
Financing	0.8	1.3	2.0	4.2	3.9	4.9	5.1	5.1
Domestic financing	0.3	0.7	0.6	1.5	0.7	-0.3	-0.4	-0.4
Bank financing	0.3	0.7	0.6	1.5	0.7	-0.3	-0.4	-0.4
Nonbank financing	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Securitization of domestic arrears	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Cash repayments of domestic debt	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
External financing	0.5	0.6	1.4	2.7	3.2	3.1	3.0	3.1
Disbursements	0.9	1.0	1.8	3.3	3.9	3.6	3.5	3.5
Amortization payments	-0.4	-0.4	-0.4	-0.6	-0.6	-0.5	-0.5	-0.5
Amortization obligations	-0.6	-0.7	-0.5	-0.4	-0.6	-0.5	-0.5	-0.5
Change in overdue obligations	0.2	0.2	0.1	-0.4	-0.3	0.0	0.0	0.0
Change in nonoverdue obligations 3/	-1.9	-1.8	-1.8	0.0	0.0	0.0	0.0	0.0
Debt relief on principal payments 2/	1.9	1.9	1.8	0.2	0.3	0.0	0.0	0.0
Residual/financing gap	0.0	0.0	0.0	0.0	0.0	2.2	2.5	2.5
Memorandum items:								
Overall balance before grants (payment-ordt)	-9.6	-8.4	-6.4	-9.4	-7.9	-8.9	-9.7	-8.6
Overall balance before grants (cash basis)	-8.2	-7.9	-7.0	-10.1	-10.8	-11.3	-11.7	-10.6
Domestic balance 4/	-2.6	-1.6	-0.3	-2.0	1.1	2.8	2.8	2.8
Revenue	23.5	24.4	23.3	23.5	27.7	27.3	26.8	26.0
Domestic-financed expenditures	26.1	26.0	23.6	25.5	26.6	24.5	24.0	23.2
Health and education outlays	9.5	...	11.2	...	...	...	...	...
Public sector average salary growth (percentage change)	1.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Wages and salaries, excluding cost of military demobilization	15.3	14.7	14.3	13.7	13.6	12.8	12.1	11.4
GDP at market prices (in millions of Djibouti Francs)	95,273	98,267	101,870	105,210	110,539	116,264	122,431	129,766

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

1/ Includes severance payments to military personnel being demobilized.

2/ Includes rescheduling of arrears on external debt payments as of end-October 1999 and external debt payments falling due during November 1, 1999 to June 2002.

3/ Reflect bilateral debt cancellation (agreement signed in 1999).

4/ Total revenue (excluding grants) less total domestically-financed current and capital expenditures.

Table 4. Djibouti: Monetary Survey and Banking Sector Indicators, 1999–2006 1/

	1999	2000	2001	Est. 2002	2003	Rev. Proj.		2006
						2004	2005	
(Stocks at end-period; in millions of Djibouti francs)								
Broad money	52,021	52,608	56,569	65,437	68,751	72,312	76,148	80,710
Currency in circulation	9,289	9,207	9,370	10,188	10,704	11,258	11,856	12,566
Deposits	42,732	43,401	47,199	55,249	58,047	61,054	64,292	68,144
Demand deposits	20,986	18,704	19,275	25,327	26,610	27,988	29,473	31,238
Djibouti francs	13,253	13,273	13,688	16,304	17,130	18,017	18,973	20,109
Foreign currency	7,733	5,431	5,587	9,023	9,480	9,971	10,500	11,129
Time deposits	21,746	24,697	27,924	29,922	31,437	33,066	34,820	36,906
Djibouti francs	3,578	4,801	7,161	8,820	9,267	9,747	10,264	10,879
Foreign currency	18,168	19,896	20,763	21,102	22,171	23,319	24,556	26,027
Net foreign assets	33,725	29,945	38,412	47,269	49,797	53,300	57,059	61,362
Currency board	10,097	9,346	9,425	10,238	9,752	10,420	11,239	12,317
Assets	12,508	12,013	12,496	13,245	13,828	14,375	14,995	15,767
Liabilities	2,411	2,667	3,071	3,012	4,076	3,954	3,756	3,449
Commercial banks	23,628	20,599	28,987	37,031	40,045	42,880	45,819	49,045
Assets	31,679	29,507	35,873	44,681	47,771	50,684	53,701	57,005
Liabilities	8,051	8,908	6,886	7,650	7,727	7,804	7,882	7,961
Net domestic assets	18,296	22,663	18,157	18,168	18,954	19,012	19,089	19,348
Claims on government (net)	1,757	2,402	2,959	4,537	5,306	4,964	4,519	3,942
Central bank	1,776	2,378	2,916	3,062	4,126	4,079	3,929	3,647
Commercial banks	-19	24	43	1,475	1,180	885	590	295
Claims on nongovernment sector	30,251	32,953	28,656	27,003	27,020	27,420	27,942	28,778
Public enterprises	2,309	1,540	1,758	1,374	1,375	1,395	1,422	1,464
Private sector	27,942	31,413	26,898	25,629	25,646	26,025	26,521	27,314
Of which								
In foreign currency	7,912	11,014	6,522	6,375	6,379	6,474	6,597	6,794
Capital accounts	-11,267	-10,263	-10,432	-10,483	-10,483	-10,483	-10,483	-10,483
Other items (net)	-2,445	-2,429	-3,026	-2,889	-2,889	-2,889	-2,889	-2,889
(Change from preceding December; in percent of broad money)								
Broad money	5.2	1.1	7.5	15.7	5.1	5.2	5.3	6.0
Currency in circulation	0.4	-0.2	0.3	1.4	0.8	0.8	0.8	0.9
Demand deposits	4.0	-4.4	1.1	10.7	2.3	2.0	2.1	2.3
Time deposits	0.7	5.7	6.1	3.5	2.7	2.4	2.4	2.7
Net foreign assets	5.7	-7.3	16.1	15.7	3.9	5.1	5.2	5.7
Central bank	0.6	-1.4	0.2	1.4	-0.7	1.0	1.1	1.4
Commercial banks	5.0	-5.8	15.9	14.2	4.6	4.1	4.1	4.2
Net domestic assets	-0.5	8.4	-8.6	0.0	1.2	0.1	0.1	0.3
Claims on government (net)	-0.2	1.2	1.1	2.8	1.2	-0.5	-0.6	-0.8
Claims on nongovernment sector	2.7	5.2	-8.2	-2.9	0.0	0.6	0.7	1.1
Capital accounts	-2.2	1.9	0.4	-0.7	0.0	0.0	0.0	0.1
Other items (net)	-0.9	0.0	-1.1	0.3	0.0	0.0	0.0	0.0
Memorandum items:								
Broad money growth (percent from previous December)	5.2	1.1	7.5	15.7	5.1	5.2	5.3	6.0
Reserve money growth (percent from previous December)	4.8	-0.8	5.4	9.0	5.1	5.2	5.3	6.0
Credit growth to nongovernment (from December)	4.6	8.9	-13.0	-5.8	0.1	1.5	1.9	3.0
Public enterprises	9.2	-33.3	14.2	-21.8	0.1	1.5	1.9	3.0
Private sector	4.3	12.4	-14.4	-4.7	0.1	1.5	1.9	3.0
Money multiplier	5.20	5.3	5.4	5.7	5.7	5.7	5.7	5.7
Velocity of broad money	1.81	1.9	1.8	1.6	1.6	1.6	1.6	1.6
Dollarization of (in percent)								
Resident and nonresident deposits	63.9	63.1	59.5	58.5	...	...	...	...
Credit	28.3	35.1	24.2	24.9	...	...	...	...
Currency board cover								
GFA (percent of currency outside banks)	127.1	122.3	122.6	120.6	119.8	118.4	117.3	116.4
GFA (percent of money plus government depts.)	112.0	115.0	115.9	114.9	114.2	112.9	113.0	110.5

Sources: Djibouti authorities; and IMF staff estimates and projections.

1/ Since 1998, the monetary survey data and projections has covered three operating commercial banks and exclude data for the two commercial banks currently under liquidation.



Table 5. Djibouti: Balance of Payments, 1999–2006 (concluded)

(In millions of U.S. dollars; unless otherwise indicated)

	1998	1999	2000	2001	Est. 2002	2003	Rev. Proj.		2005
							2004	2004	
Memorandum items:									
In percent of GDP									
Merchandise trade account	-35.1	-34.0	-35.2	-31.2	-33.9	-38.5	-43.1	-43.1	-40.7
Current account	-0.6	-0.6	-7.2	-4.3	-6.2	-5.3	-13.0	-12.4	-11.1
Capital account 7/	-0.8	2.0	3.9	12.1	15.1	6.6	16.0	15.5	14.4
Overall balance	-1.4	1.5	-3.3	3.0	9.0	1.3	3.0	3.1	3.3
Central bank net foreign assets	55.1	56.9	52.1	53.1	57.7	55.0	58.7	63.3	69.4
In number of months of imports 8/		2.6	2.2	2.4	2.4	2.0	1.8	1.9	2.0
Central bank gross foreign assets	64.4	70.4	67.6	70.3	74.5	77.8	80.9	84.4	88.7
In number of months of imports 8/	2.9	3.2	2.9	3.2	3.1	2.8	2.5	2.5	2.6
Central bank foreign liabilities	9.3	13.5	15.5	17.2	16.9	22.8	22.2	21.0	19.3
Of which 9/									
IMF	8.5	12.7	13.4	15.5	14.5	19.0	18.7	17.9	16.3
Arab Monetary Fund	0.7	0.7	1.5	1.7	2.4	3.9	3.5	3.2	3.0
Commercial banks' net foreign assets	118.9	132.9	115.9	163.1	208.4	225.3	241.3	257.8	276.0
In months of imports 8/		6.1	4.9	7.4	8.6	8.1	7.4	7.6	8.1
Commercial banks' gross foreign assets 10/	170.2	178.3	166.0	201.9	251.4	268.8	285.2	302.2	320.8
In months of imports 8/	7.6	8.1	7.1	9.1	10.4	9.6	8.8	8.9	9.4
Commercial banks' foreign liabilities	89.9	45.3	50.1	38.7	43.0	43.5	43.9	44.3	44.8
Debt service ratios 11/									
In percent of current account receipts									
Obligations basis before rescheduling	5.5	6.3	7.9	5.8	6.1	5.3	5.1	4.9	5.1
Obligations basis after rescheduling	4.9	5.4	4.8	5.5	5.5	5.3	5.1	4.9	5.1
In percent of exports of locally produced goods and nonfactor services									
Obligations basis before rescheduling	8.3	9.4	11.9	7.6	8.1	7.7	7.3	7.2	7.2
Obligations basis after rescheduling	7.5	8.2	7.3	7.3	7.3	7.7	7.3	7.2	7.2
Official debt									
In millions of U.S. dollars	337.0	336.9	369.9	373.7	395.3	413.6	444.5	471.2	498.4
In percent of GDP	65.5	62.8	66.9	65.2	66.8	66.5	68.0	68.4	68.3
Stock of public sector overdue obligations	5.4	10.9	7.7	9.9	9.4	0.0	0.0	0.0	0.0

Sources: Data provided by the authorities; and IMF staff estimates and projections.

1/ For 2000, data include imports of cranes for the port of Djibouti.

2/ Excluding privatization receipts.

3/ Excluding disbursements from the IMF and Arab Monetary Fund in 2001 and 2002.

4/ Based on three banks since 1998.

5/ Reflect the bilateral debt cancellation agreement signed in 1999 on the terms of reference agreed between the members of the Paris Club and the Djibouti authorities for the period 2000–02 and the terms of reference agreed between the Saudi Development Fund and the Djibouti authorities for the period 2001–06.

6/ Figures for the 1999–2001 period correspond to Italian debt forgiveness, and for 2002 correspond to a partial debt cancellation with Paris hospitals (Hospital Public Assistance).

7/ Including errors and omissions.

8/ Imports of goods for domestic use and nonfactor services.

9/ Includes Poverty Reduction and Growth Facility and expected Arab Monetary Fund resources.

10/ From 1998 onwards based on gross foreign assets of three operating banks only.

11/ Public and publicly guaranteed debt. The higher-than-programmed debt service ratio in 2001 reflects significant payments made by the authorities on reschedulable obligations, particularly on those due by public enterprises.



Table 6. Djibouti: Selected Economic Indicators—Initial Poverty Reduction and Growth Facility (PRGF) Projections and Actual Outcome, 1999–2002

	Initial PRGF Projections (EBS/99/190)				Actual Outcome			
	1999	2000	2001	2002	1999	2000	2001	2002
(Percentage change, unless otherwise indicated)								
<b>National income and prices</b>								
Nominal GDP (in millions of Djibouti francs)	94,352	98,486	103,641	110,197	95,273	98,267	101,870	105,210
GDP at current prices	3.5	4.4	5.2	6.3	4.4	3.1	3.7	3.3
GDP at constant prices	1.4	2.3	3.2	4.3	2.2	0.7	1.9	2.6
Consumer prices (annual average) 1/	2.0	2.0	2.0	2.0	2.0	2.4	1.8	0.6
(In percent of GDP)								
<b>Investment and Saving</b>								
Investment	11.7	13.8	13.6	13.5	8.8	12.2	8.3	10.2
Saving								
Domestic saving	-11.7	-9.5	-7.0	-4.8	-5.7	-7.4	-3.7	-4.6
National saving	-9.4	-7.3	-4.9	-2.8	8.2	5.1	3.9	4.0
<b>Consolidated government operations</b>								
Total revenue and grants	34.4	36.2	34.9	34.5	30.9	31.0	28.2	29.4
Total expenditures	34.8	35.5	34.4	35.0	33.1	32.8	29.7	32.9
Overall balance (payment order basis)	-0.4	0.7	0.5	-0.5	-2.2	-1.8	-1.4	-3.5
Change in arrears (decrease -)	-1.2	-4.5	-4.3	-2.8	1.3	0.5	-0.6	-0.7
Overall balance (cash basis)	-1.6	-3.8	-3.9	-3.3	-0.8	-1.3	-2.0	-4.2
Government domestic arrears (stock) 2/	20.8	13.6	7.6	3.2	29.3	29.6	28.9	27.8
(Change from preceding December; in percent of broad money) 3/								
<b>Money and credit</b>								
Money and quasi-money	2.2	5.4	5.8	6.4	5.2	1.1	7.5	15.7
Net foreign assets	-0.9	0.5	0.4	0.8	5.7	-7.3	16.1	15.7
Net domestic assets	3.1	5.0	5.4	5.6	-0.5	8.4	-8.6	0.0
Of which								
Claims on the central government (net)	0.6	2.2	2.1	1.7	-0.2	1.2	1.1	2.8
Claims on nongovernment sector	6.1	2.8	3.3	3.9	2.7	5.2	-8.2	-2.9
<b>Interest rates</b>								
Lending rates	...	...	...	...	7.0–14.0	12.1–14.1	10.8–11.7	8.5–11.4
Deposit rates	...	...	...	...	2.5–5.1	3.8–5.0	2.5–3.2	1.0–1.5
(In millions of U.S. dollars)								
<b>External sector</b>								
Current account	-32.9	-35.9	-35.5	-33.4	-1.9	-39.7	-24.9	-36.5
Trade balance	-177.9	-184.2	-183.9	-190.4	-182.4	-194.8	-178.7	-200.5
Transfers (net)	70.8	73.3	65.4	61.5	62.7	53.1	31.1	40.6
Capital account	17.6	21.7	21.6	22.3	-1.2	30.7	10.2	34.9
Errors and omissions (including other private capital)	0.0	0.0	0.0	0.0	12.1	-9.1	54.6	54.7
Overall balance	-15	-14.2	-14.0	-11.0	7.9	-18.1	39.9	53.0
<b>Memorandum items:</b>								
Currency board gross foreign assets								
Monetary and LOLR cover (in percent)	118.1	116.9	117.3	116.5	111.7	114.9	115.8	114.9
As a ratio to currency issue	1.2	1.2	1.2	1.2	1.3	1.2	1.2	1.3
Current account (in percent of GDP)	-6.2	-6.5	-6.1	-5.4	-0.6	-7.2	-4.3	-6.2
Overall balance (in percent of GDP)	-2.8	-2.6	-2.4	-1.8	1.5	-3.3	3.0	9.0
Official external debt 4/								
After rescheduling (in percent of GDP)	68.8	67.7	66.9	65.4	62.8	66.9	65.2	66.8
Debt service ratio								
To exports of goods and services 5/								
Obligations basis after rescheduling	2.6	6.1	5.4	4.9	8.2	7.3	7.3	7.3

Sources: Djibouti authorities; and IMF staff estimates and projections.

1/ Starting in 1999 actual data and projections for 2003–06 are based on the official CPI introduced in April 1999.

2/ Domestic arrears data from 1999 include wage arrears, arrears to private and public supplies for goods and services, preliminary estimates of arrears to the pension funds, and the arrears of the liquidated public agency that formerly controlled the grain trade that have been assumed. Data for 2000 are derived from the surveys on domestic arrears conducted by the World Bank and the European Union.

3/ Beginning in 1998, data include only three operating banks and exclude two closed banks which are being liquidated.

4/ Public and publicly guaranteed debt of the central government and the public enterprise sector. Data reflect the bilateral debt cancellation agreement signed in 1999, the terms of reference agreed between the members of the Paris Club and the Djibouti authorities for the period 2000–02, and the terms of reference agreed between the Saudi Development Fund and the Djibouti authorities for the period 2001–06.

5/ Exports of locally produced goods and nonfactor services.

Table 7. Djibouti: External Financing Requirements—Initial Poverty Reduction and Growth Facility (PRGF) Projections and Actual Outcome, 1999–2002

(In millions of U.S. dollars)

	Initial PRGF Projections (EBS/99/190)				Total Flows Initial PRGF	Actual Outcome				Total Flows Actual
	1999	2000	2001	2002		1999	2000	2001	2002	
External financing requirements	102.3	100.2	90.8	84.3	377.6	84.7	113.4	71.8	101.5	371.3
Current account excluding										
official transfers 1/	77.3	83.4	75.0	69.0	304.7	71.4	99.7	61.8	80.9	313.8
Amortization obligations	12.6	13.2	12.2	11.6	49.6	13.1	14.7	11.7	10.6	50.2
Change in arrears (decrease +)	8.9	0.0	0.0	0.0	8.9	-5.4	3.2	-2.2	5.5	1.1
Net official reserves (increase +) 2/	3.5	3.6	3.6	3.7	14.4	5.5	-4.2	0.4	4.5	6.3
Sources of financing	102.3	100.2	90.8	84.3	377.6	84.7	113.4	71.8	101.5	371.3
Official grants	44.7	47.5	39.4	35.7	167.3	69.5	60.0	37.0	44.4	210.8
Loan disbursements	26.9	28.6	27.1	27.0	109.6	8.1	39.9	19.7	33.5	101.2
Foreign direct investment	3.4	6.3	6.7	7.0	23.4	4.2	3.3	2.2	5.0	14.8
Other private capital net (including errors and omissions)	1.4	-3.9	-3.9	-3.9	-10.3	-3.4	5.9	7.4	9.4	19.3
Debt relief	20.1	6.6	8.8	5.8	41.3	2.5	0.0	0.7	1.6	4.8
Program financing	5.8	15.1	12.7	12.7	46.3	3.8	4.3	4.8	7.5	20.5
IMF (PRGF) 3/	3.8	7.7	7.7	7.7	26.9	3.8	3.6	4.6	0.0	12.0
World Bank	0.0	5.0	5.0	5.0	15.0	0.0	0.0	0.0	5.0	5.0
African Development Bank	1.6	1.6	0.0	0.0	3.2	0.0	0.0	0.0	1.9	1.9
Arab Monetary Fund	0.4	0.8	0.0	0.0	1.2	0.0	0.8	0.2	0.7	1.6
Residual gap	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Sources: Djibouti authorities; and IMF staff estimates.

1/ Official transfers exclude grants to government and public enterprises, but include nonresident income tax and technical assistance.

2/ Includes changes in liabilities to the IMF.

3/ The last disbursement under the PRGF of \$6.2 millions was made in early 2003.

Table 8. Djibouti: Medium-Term Macroeconomic Framework, Saving, and Investment Balances, 1999–2006

	1999	2000	2001	Est. 2002	Rev. Proj.			
					2003	2004	2005	2006
(Average percentage change)								
Economic growth and prices								
Real GDP	2.2	0.7	1.9	2.6	3.0	3.1	3.2	3.9
Consumer prices (period average)	2.0	2.4	1.8	0.6	2.0	2.0	2.0	2.0
(In percent of GDP)								
Gross domestic expenditures	114.5	119.6	112.0	114.8	118.7	124.9	125.3	122.8
Consumption expenditure 1/	105.7	107.4	103.7	104.6	106.9	104.8	104.3	102.3
Central government	26.1	25.8	23.4	25.1	26.4	24.3	23.0	21.7
Nongovernment	79.6	81.6	80.3	79.5	80.5	80.5	81.3	80.7
Investment 2/	8.8	12.2	8.3	10.2	11.8	20.1	21.0	20.5
Government	3.1	2.7	2.5	3.7	4.3	7.1	8.5	8.1
Nongovernment	5.7	9.6	5.8	6.5	7.4	13.0	12.5	12.4
Domestic savings	-5.7	-7.4	-3.7	-4.6	-6.9	-4.8	-4.3	-2.3
Government	-6.5	-5.7	-3.9	-5.7	-3.6	-1.8	-1.2	-0.5
Nongovernment	0.8	-1.7	0.2	1.1	-3.4	-3.0	-3.1	-1.8
Net current transfers and factor income	14.0	12.4	7.6	8.6	13.4	11.9	12.9	11.7
Net current transfers	11.7	9.6	5.4	6.9	7.8	7.3	7.5	6.3
Net factor income	2.3	2.9	2.2	1.8	5.6	4.6	5.4	5.4
National savings 3/	8.2	5.1	3.9	4.0	6.5	7.1	8.6	9.4
Saving/investment gap 4/	-0.6	-7.2	-4.3	-6.2	-5.3	-13.0	-12.4	-11.1
Memorandum items:								
Central government finances								
Revenue and grants	30.9	31.0	28.2	29.4	34.5	33.7	33.4	31.5
Current expenditure	30.0	30.1	27.2	29.2	31.2	29.1	27.9	26.6
Capital expenditure	3.1	2.7	2.5	3.7	4.3	7.1	8.5	8.1
Overall balance (payment order)	-2.2	-1.8	-1.4	-3.5	-1.0	-2.5	-3.1	-3.2
Real GDP per capita (Change in percent)	-0.8	-2.2	-1.1	-0.4	0.0	0.1	0.2	0.9
Nominal GDP (In millions of Djibouti francs)	95,273	98,267	101,870	105,210	110,539	116,264	122,431	129,766
Nominal GDP (In millions of U.S. dollars)	536.1	552.9	573.2	592.0	622.0	654.2	688.9	730.2

Source: Djibouti authorities; and IMF staff estimates and projections.

1/ The high level of consumption and negative domestic savings are permitted by large inflows of external grants.

2/ Equals gross capital formation.

3/ National savings is defined as domestic savings plus net current transfers and factor income from abroad.

4/ The saving/investment gap corresponds to the external current account balance including current grants.

**DJIBOUTI: RELATIONS WITH THE FUND**  
(As of September 30, 2003)

**Membership Status:** Joined 12/29/78; Article VIII

<b>General Resources Account:</b>	<u>SDR million</u>	<u>Percent of Quota</u>
Quota	15.90	100.00
Fund holdings of currency	15.17	95.38
Reserve position in Fund	1.10	6.92

<b>SDR Department:</b>	<u>SDR million</u>	<u>Percent of Allocation</u>
Net cumulative allocation	1.18	100.00
Holdings	0.13	11.01

<b>Outstanding Purchases and Loans:</b>	<u>SDR million</u>	<u>Percent of Quota</u>
Stand-by arrangements	0.37	2.30
PRGF arrangements	13.63	85.72

**Financial Arrangements:**

<u>Type</u>	<u>Approval Date</u>	<u>Expiration Date</u>	<u>Amount</u>	
			<u>Approved</u>	<u>Drawn</u>
			<u>(SDR million)</u>	<u>(SDR million)</u>
PRGF	10/18/1999	01/17/2003	19.08	13.63
Stand-by	04/15/1996	03/31/1999	8.25	7.27

**Projected Obligations to the Fund:** (SDR million; based on existing use of resources and present holdings of SDRs):

	<u>Forthcoming</u>				
	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>
Principal	0.24	0.12	0.55	1.09	1.82
Charges/Interest	0.04	0.08	0.08	0.08	0.07
Total	0.28	0.21	0.63	1.17	1.89

### **Safeguards Assessments**

Under the Fund's safeguards assessment policy, the Central Bank of Djibouti (BCD) is subject to the transitional procedures with respect to the Poverty Reduction and Growth Facility (PRGF) arrangement, which was approved on October 18, 1999 and expired on January 17, 2003. The transitional procedures require a review of only the BCD's external audit mechanism. This assessment determines whether the BCD publishes annual financial statements that are independently audited in accordance with internationally-accepted standards.

The external audit assessment was completed on July 24, 2001. The assessment concluded that the BCD's current external audit mechanism may not be compliant with the international auditing standards promulgated by the International Federation of Accountants, and recommendations had been made to the authorities, as reported in "Djibouti: Report on the External Audit Mechanism." In response to staff recommendations, the BCD hired, in August 2002, external auditors from Ernst & Young to audit the 1999, 2000, and 2001 accounts. The audit of BCD accounts was completed by year-end 2002. Beginning 2003, the BCD will have its accounts audited on a yearly basis in accordance with international auditing standards.

### **Exchange arrangements**

Djibouti has a currency board arrangement. The Djibouti franc is pegged to the U.S. dollar at the rate of DF 177.721 = \$1. Djibouti maintains an exchange system that is free of restrictions on payments and transfers for all international current and capital transactions.

### **Article IV Consultation**

Djibouti is on an annual consultation cycle. Discussions for the 2001 Article IV consultation were held in Djibouti from September 9 to 22, 2000, November 1 to 15, 2000, March 18 to April 1, 2001, and June 15 to 28, 2001, and in Paris from October 6 to 13, 2001 in conjunction with discussions on the second review under the PRGF arrangement. The consultation was concluded and the second review under the PRGF arrangement was approved by the Executive Board on November 28, 2001. Subsequently, the last and third PRGF review was concluded and approved by the Executive Board on December 20, 2002.

### **FSAP Participation, ROSC, and OFC Assessment**

Djibouti has not participated in any of the above-mentioned exercises.

**Technical Assistance**

FAD—Budget control and cash management of the treasury	April 2000
FAD—Direct tax reform	September 2000
FAD/MED—Budget control and cash management of the treasury	February 2001
STA—Government finance statistics	May 2001
STA—National accounts and balance of payments statistics	January 2002
FAD—Tax administration and possible introduction of a VAT	April 2002
MAE—Banking supervision	December 2002
STA—Balance of payment statistics	November 2003

**Resident Representative**

A resident representative has been stationed in Djibouti since October 1998.

**DJIBOUTI: RELATIONS WITH THE WORLD BANK**  
(As of September 8, 2003)

**Partnership in Djibouti's Development Strategy**

1. Relations between the World Bank (the Bank) and the government of Djibouti are closer, and the Bank has been more active in Djibouti since operational responsibilities were transferred in October 1999 from Africa Region to the Middle East and North Africa Region of the Bank. Government counterparts have a clearer understanding of the Bank's assistance, and more realistic expectations of future support from the Bank.
2. The Bank, in consultation with the government of Djibouti, developed the country assistance strategy (CAS), which the Executive Board endorsed in December 2000 covering the FY2001–03 period. The objectives of the CAS are being met through two main pillars: (a) direct interventions to reduce poverty, which would focus on reversing the extremely low enrollment rate in education while addressing the needs in health—particularly those related to the epidemic rate of HIV/AIDS—and preparing a program of assistance for vulnerable groups to cushion the impact of adjustment; and (b) measures to provide the basis for growth and employment generation supported through structural reforms, and develop associated infrastructure services for the port of Djibouti.
3. In the context of the Poverty Reduction and Growth Facility, the Fund assists the government in addressing its economic stabilization and financial reform issues. In conjunction with this anti-poverty oriented program, which covers 1999–2002, the Bank approved, in December 2001, a fiscal consolidation credit (FCC)—a complementary structural reform support—in the amount of \$10 million equivalent. The first tranche of the FCC (about \$5 million) was released in March 2002.
4. The government is still expected to meet several conditions for the release of the second tranche of the FCC; the conditions are in three critical areas as follows: (a) reforms of pension funds (operating of the National Council for Social Security), audit and update of *Office de Prévoyance Sociale* files for participants and beneficiaries, and a study followed by an action plan for the management of funds' reserves); (b) containing the wage bill through the merging of personnel and payroll files, and the demobilization of 1,000 extra military personnel or ex-combatants; and (c) financial audits of the three remaining public enterprises (water, power, and telecommunications). In light of these delays, the government has requested, and International Development Association (IDA) has approved, the extension of the FCC's closing to October 31, 2003.
5. As efforts are made to address the country's poverty issues, the Bank and the Fund will continue to collaborate in their respective areas of assistance to the government of Djibouti. The Fund will continue to lead the policy dialogue on macroeconomic policy (fiscal, monetary, and exchange rate) and on areas of structural reforms (fiscal management

and control, banking supervision and banking sector issues, and tax reform). The Bank will concentrate on the policy dialogue relating to other structural reforms, including pension funds, public enterprises sector and privatization, and poverty monitoring and evaluation. Areas of close collaboration include the Poverty Reduction Strategy Paper (PRSP) under preparation and public expenditure management.

### **Bank Group Strategy**

6. The Bank assistance strategy for Djibouti is being pursued through: (a) structural reforms, including public enterprise restructuring, pension reform, and public expenditure management reform to improve the efficiency and effectiveness of public spending; (b) poverty reduction, including the expansion of basic education, health, and strengthening the social safety net; and (c) economic growth by assisting Djibouti in taking maximum advantage of its infrastructure and services.

7. The ongoing technical assistance project (PATARE) also supports the government's reform program. The closing date of PATARE has been extended by one year (from December 2002 to December 31, 2003) to enable the completion of project activities as they relate to the reform program supported by the FCC.

8. The Bank's future support to Djibouti is embedded in the PRSP, expected to be finalized in FY2004; and the CAS update, also planned for FY2004. The Bank endorsed the Interim PRSP in November 2001. Progress has been made in the preparation of the full PRSP. The first phase of the poverty diagnostics and analysis survey (EDAM II Social Indicators) has been completed and preliminary results have been tabulated. The Bank and the UNDP provide technical assistance to analyze the survey results for policy recommendations. The Bank will complete a Water Sector Strategy for Djibouti in FY2004, as well as a Country Financial Accountability Assessment and a Public Expenditure Review.

### **Status of the Portfolio**

9. As of July 31, 2003, IDA had approved 16 projects for Djibouti valued at about \$148.6 million of which 15 are investment projects and one is an adjustment operation. Of this amount, about \$91.7 million has been disbursed and \$53.8 million undisbursed.

10. The current portfolio has seven active projects valued at \$94.3million, of which 49.6 percent, by value, is for health and social development; 22.3 percent for transport and infrastructure; 10.6 percent for education; 6.9 percent for technical assistance; and the remaining 10.6 percent is for fiscal consolidation (adjustment operation). In addition, the Bank approved one IDF grant in FY2002 of \$138,000 for capacity building to enhance Djibouti's debt management.

11. The portfolio ended the fiscal year 2003 (FY03) with a rather mixed performance. The disbursement ratio hit a record high of over 24 percent compared to the regional target of about 21 percent. On the other hand, the portfolio had 35 percent (by value) of projects at



risk. This was due to the poor performance of two projects (FCC and International Road Corridor). We expect the government to meet the conditions for the release of the FCC's second tranche; and also address the financial management issues affecting the International Road Corridor project.

### **Bank-Fund Collaboration in Specific Areas**

12. In addition to the overall assistance to Djibouti through lending, country analytical work, and technical assistance, the Bank supports policy reforms in close collaboration with the Fund in the following areas:

- **Public Expenditure Management.** The Fund and Bank jointly emphasize the urgent need to further improve public expenditure management, accountability, and transparency. The two institutions support policy reforms in the areas of budget formulation, execution, and monitoring. On budgetary reforms, emphasis has been placed on: (a) the implementation of an improved expenditure nomenclature to track more easily the poverty reduction effort; (b) the need to accelerate the execution of expenditure, notably in social sectors; and (c) the modernization of the public procurement system. On budget reporting, the Bank and Fund will support Djibouti in its efforts to strengthen the capacity of audit institutions and produce budget execution laws in a timely fashion. The ongoing public expenditure review undertaken by the Bank this fiscal year (FY03) will contribute to future support on this area.
- **Poverty Reduction Strategy Paper (PRSP).** Since the Boards of the IMF and the Bank endorsed the Interim PRSP in November 2001, the staff of both institutions have been working closely to help the government finalize its PRSP. The final validation meeting with the civil society took place in late July 2003. The authorities are planning a presentation of the PRSP to the Bank and Fund's Boards by October 30, 2003. Bank and Fund staff have provided comments on the first drafts of the paper. There are still some shortcomings, in particular regarding the consistency between the investment program, the proposed sectoral strategies, the growth and poverty expected outcomes, and the fiscal framework viability.

## DJIBOUTI: STATISTICAL ISSUES

### Outstanding Statistical Issues

1. Statistical data suffer, although unevenly, from deficiencies with regard to their quality, coverage, periodicity, timeliness, and dissemination. The situation is especially critical for balance of payments, domestic debt and arrears, and real sector. These weaknesses continue to hamper policy analysis and monitoring. Statistics in Djibouti are compiled by different institutions, and data reconciliation among these sources is limited.
2. Recent developments, however, indicate an increasing awareness of the importance of statistics among government officials who are eager to take measures needed to improve the situation. Among the most encouraging initiatives, the authorities introduced a consumer price index (CPI) in April 1999, which was developed in collaboration with the *Observatoire économique d'Afrique subsaharienne* and published in October 1999. In addition, updated national account estimates for 1990–98 were developed in collaboration with the African Development Bank. More recently, the authorities created the Directorate for Statistics and Population Studies (DISEP) by merging the National Directorate of Statistics (DINAS) and the Central Bureau of Census in order to enhance capacity of the statistical system and efficient use of available resources. However, significant work remains to bring statistical data up to internationally accepted standards.

### National Accounts

3. The existing national accounts estimates follow the *System of National Accounts 1968*. The 1998 revision led to some improvements in the methodology of compilation. A supply side approach remains the mainstay of the compilation method and there continues to be a focus on main GDP aggregates. However, this revision fell short of correcting the serious defects in Djibouti's national accounts arising from the underlying weaknesses in basic data sources and lack of resources. These factors also explain, in part, the limited progress made in implementing the January 2001 statistics (STA) mission recommendations.

### Prices

4. The CPI is the only available measure of inflation in Djibouti. Under the stand-by arrangement (SBA), the CPI compiled by the French government for French expatriate residents in Djibouti was used as a proxy for a Djibouti CPI. This index, however, was of weak quality and not representative of Djibouti's consumption basket and, therefore, in late 1998 the Fund staff began to track Djibouti price developments beginning in 1994 by utilizing: (a) sub-indices from the French CPI—that were representative of Djibouti consumption; and (b) weights derived from a recent Djibouti household survey. The new national CPI is now considered to be the official measure of monthly price developments since April 1999.

### **Government Finance**

5. Although data compilation improvements were made under the SBA, the fiscal data remains weak as does coordination among government agencies in producing internally consistent data. Improvements in both areas are needed. The coordination unit in the ministry of economy and finance (MOEF), established in July 1998 to improve data coverage and timeliness, has not yet succeeded in fulfilling its mandate in a satisfactory manner. This is due, in part, to inadequate staffing and insufficient support from higher levels within the government. Among the encouraging initiatives taken, was the recent computerization of the treasury accounts, which will significantly improve the coverage, quality, timeliness, consolidation, and consistency of cash management data. Additional efforts are needed to improve the compilation of budgetary data, particularly at the institutional level. Limited progress was made in this area as most of the May 2001 STA mission recommendations are still not implemented. Another encouraging step is the improvement of data on domestic budgetary arrears through the comprehensive audit of these arrears in 2002 with assistance from the European Union and the World Bank. Foreign-financed capital expenditure and some foreign-financed current expenditures and their financing (namely grants and loans) have been reported since the 1999 budget.

### **Monetary Accounts**

6. To improve the quality of monetary data, commercial banks were instructed in July 1999 to initiate a program for accurately identifying the residency status of their customers and to report balance sheet data on this basis to the Banque Nationale de Djibouti (BND)<sup>1</sup> beginning with the end-December 1999 reporting period. The BND maintains a computerized system for compiling monetary statistics and began to publish a quarterly bulletin in 1995, which includes the central bank balance sheet and the monetary survey. The BND also started issuing a monthly bulletin in 2001. For program purposes, the Fund staff uses monetary data covering the three operating commercial banks. This data excludes the assets and liabilities of two banks in liquidation.

### **Interest Rates**

7. Previously, commercial banks reported only their end-quarter minimum and maximum deposit and lending rates. To enhance transparency and foster competition in domestic financial markets, the BND, in August 1999, instructed all banks to publicly post and update, at least weekly, their full interest rate structure and to report this information to the BND on a weekly basis. The data on the structure of interest rates have now become available.

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<sup>1</sup> Banque centrale de Djibouti before 2002.

### External Sectors

8. The reliability of balance of payments data is hindered by deficiencies in merchandise trade data provided by the DISEP (DINAS before 2002) and unreliable procedures (nonrepresentative surveys, crude assumptions, etc.) used to estimate the other components of the balance of payments, particularly transport and insurance costs. Merchandise trade data compiled by the DISEP using customs data are deemed to significantly underestimate imports and exports and do not fully capture transactions recorded by customs. A number of imported goods are recorded c.i.f., whereas others are recorded f.o.b., in particular if costs of insurance and freight are not presented separately on the invoice. Trade data are reported annually and quarterly usually with a delay of six months. Data on private capital flows are deficient as commercial banks do not provide information to the BND on the nature of foreign exchange transactions. Moreover, information on the residency status of the account holders is weak, which hinders the compilation of private capital flows. Data on foreign grants and loans received by ministries, public sector enterprises, and other entities are now better centralized and coordinated at the MOEF.

9. The external debt data produced by the *Service de la Dette* (SD) of the MOEF are incomplete, lack consistency and accuracy, and are not sufficiently detailed. Data on loan agreements, disbursements, and debt service payments are not available at the SD in a timely and regular manner, particularly for public enterprises. To improve this situation, the authorities launched, in 2002, a project to improve the database on external debt with financial and technical assistance from the World Bank and UNCTAD. The new system became fully operational in mid-2003, following a comprehensive inventory of all external loans contracted or guaranteed by the government and appropriate training of staff. This system is expected to replace the old one (Excel worksheets) by end-2003 and a revised external debt database will be established covering the period 1999 onward.

10. A technical assistance mission in balance of payments is visiting Djibouti (November 3–17, 2003) to conduct a review of the progress in implementing the recommendations by the previous mission (January 20–February 2, 2002), review the current collection, compilation, and dissemination of statistics and to propose measures to address shortcomings noted above.

**Djibouti: Core Statistical Indicators as of End-October 2003 (some of the series)**

	Exchange Rates	International Reserves	Reserve/ Base Money	Central Bank Balance Sheet	Broad Money	Interest Rates	Consumer Price Index	Exports/ Imports	Current Account Balance	Overall Government Balance	GDP/ GNP	External Public Debt Service Stock	
Date of latest Observation	October 2003	April 2003	August 2003	August 2003	August 2003	August 2003	December 2002	December 2002	December 2002	April 2003	December 2002 1/	March 2003	December 2002
Date Received	November 2003	June 2003	October 2003	October 2003	October 2003	October 2003	February 2003	February 2003	February 2003	May 2003	February 2003	May 2003	February 2003
Frequency of Data 2/	M	M	M	M	M	Q	M	Q	A	M	A	Q	A
Frequency of Reporting	M	M	M	M	M	Q	M	Q	A	M	A	Q	A
Source of data	Central Bank	Central Bank	Central Bank	Central Bank	Central Bank	Commercial Banks	DINAS/ Ministry of Finance	DINAS/ Central Bank	DINAS/ Central Bank	Ministry of Finance	DINAS/ Ministry of Finance	Ministry of Finance	Ministry of Finance
Mode of reporting	Fax/ Cable to IMF	Fax/ Cable to IMF	Fax/ Cable to IMF/ E-mail	Fax/ Cable to IMF/ E-mail	Fax/ Cable to IMF/ E-mail	Fax/ Cable to IMF or Mission/ E-mail	Fax Cable to IMF or Mission	Fax Cable to IMF or Mission	Fax Cable to IMF or Mission	Fax Cable to IMF or Mission	Fax Cable to IMF or Mission	Mission	Mission
Confidentiality 3/	C	C	C	C	C	C	C	C	C	C	C	C	C

1/ GDP data is entirely estimated by the staff on the basis of partial data, provided by the authorities.

2/ D = Daily; W = Weekly; M = Monthly; Q = quarterly; A = Annual.

3/ C = Unrestricted.

## DEBT SUSTAINABILITY ANALYSIS

1. The reform program envisaged by the authorities to improve infrastructures, increase access to water, reestablish the financial viability of public enterprises, and implement a new social sector strategy is expected to put pressure on spending, thus raising the question of the risks to Djibouti's fiscal and external sustainability over the medium term. This appendix reviews the staff's baseline projections for Djibouti's domestic and external debts, and assesses the impact of shocks to key macroeconomic variables.

### I. THE MEDIUM-TERM FISCAL VIABILITY

#### A. Medium-Term Outlook

2. Over the next few years, in addition to facing pressures for more outlays, the government of Djibouti will have to implement fiscal reforms in line with commitments under international trade agreements,<sup>20</sup> which would affect the revenue capacity of the country. In view of these developments, adequate management of public finances is critical to maintaining fiscal sustainability and the integrity of the currency board arrangement.<sup>21</sup>

3. The baseline macroeconomic scenario underpinning the fiscal projections prepared by staff in collaboration with the authorities assumes an average real GDP growth rate of 3.8 percent a year over the period 2003–08 and a negative real interest rate on government debt of about half a percent.<sup>22</sup> The medium-term fiscal framework incorporates new streams of resources expected from bilateral donors as well as new spending envisaged by the authorities to fund poverty alleviation actions and to repay domestic debt. It is assumed, in particular, that the stock of domestic arrears will be cleared according to the 10-year plan prepared by the ministry of finance, and that up to 70 percent of the additional resources needed to cover the investment program will be mobilized in the form of loans. At the same time, the wage bill and some expenditure in goods and services (including utility bills) would decline as a percentage of GDP.

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<sup>20</sup> Under the Common Market for Eastern and Southern Africa Regional Trade Arrangement, Djibouti is expected to introduce, as of January 2004, a common external tariff. In the same vein, the authorities are planning to put in place a value-added tax (VAT) by January 2006.

<sup>21</sup> It is assumed that Djibouti will maintain its currency board arrangement with the same parity to the U.S. dollar.

<sup>22</sup> Under these assumptions, a government sector primary deficit of 3.5 percent of GDP would keep the government debt ratio unchanged (compared with a historical average of 5.1 percent of GDP during the past decade).

4. Reflecting all these assumptions, the primary deficit would rise in the initial years up to 2.7 percent of GDP before declining well below 2 percent of GDP. Accordingly, the government debt ratio would decline from 79 percent at end-2002 to about 61 percent of GDP by 2008 (a level still high by developing countries standards).

### **B. Sensitivity Test on Government Debt**

5. With the uncertainty surrounding the growth path, interest rates, and spending, a sensitivity analysis was conducted to assess the impact of shocks arising from lower growth (at historical average minus two standard deviations in 2003 and 2004, equivalent to a GDP decline of 6.7 percent each year); real interest rates (at historical average plus two standard deviations in 2003 and 2004, interest rates at an average of -0.8 percent); and primary balance (at historical average minus two standard deviations in 2003 and 2004, equivalent to a deficit of 15 percent of GDP).

6. The results of the sensitivity analysis (Table 1 and Figure 1 of Attachment I) indicate that a deviation in the primary balance would pose serious risks to fiscal sustainability, as could be expected, resulting in a government debt ratio 21 percentage points higher by 2008 than in the baseline. In the case of a GDP shock, the government debt ratio would be 15 percentage points higher. The most significant outcome was generated by setting real GDP growth, real interest rate, and the primary balance at their historical values. In this case, the government debt ratio would increase dramatically to reach 97 percent in 2008, which is 36 percentage points higher than in the baseline scenario. These results underscore the vulnerability of the fiscal accounts to shocks, and the need for the authorities to stand ready to introduce measures in order to maintain financial stability and sustain economic growth.

## **II. EXTERNAL SECTOR**

### **A. Medium-Term Outlook**

7. Under the assumption of relatively higher growth prospects and rising public consumption and investment, the baseline shows a marked increase in imports of goods and services, and a widening current account deficit of the balance of payments. In addition, it is assumed that up to 70 percent of the not-yet identified financing needs associated with the public investment program would be covered with loans. Under these assumptions, the total external debt ratio to GDP would remain broadly constant during the projection period at between 67 and 69 percent. This level is high in comparison with the average ratios of 60 percent in Africa and 40 percent of GDP in developing countries. The payment of debt service would also absorb on average about 7 percent of exports of locally produced goods and non factor services during 2003–08.<sup>23</sup>

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<sup>23</sup> The baseline scenario assumes that new loans (about 70 percent of the not yet identified financing needs of the public investment program) are amortized over a period of 12 years and would be serviced at an average interest rate of 2.5 percent a year.

### B. Sensitivity Tests on External Debt

8. Concerns about the fragility of Djibouti's external position are illustrated below by conducting different stress tests. The results of these tests show that, though with varying magnitudes, the presence of adverse temporary shocks to key macroeconomic variables (real GDP growth, GDP deflator, interest rate on external debt, and the current accounts of the balance of payments), significantly raises the risks to external sustainability and could jeopardize the implementation of the medium-term framework.

9. Most stress tests (Table 2 and Figure 2 of Attachment I) show that temporary shocks would shift the external debt-to-GDP ratio (external debt ratio) upward by at least 10 percentage points during 2003–08, and that further adjustments would be needed to restore pre-shock levels. The real GDP stress test (Test 3) has the highest impact. In the event of a sharp decline in real GDP by 6.7 percent in 2003 and 2004 (Test 3), the external debt ratio would increase by about 15 percentage points by 2005 before declining slowly thereafter. A sharp deterioration in the current account would also have a large impact (Test 5). Assuming that the current account deficit deteriorates to 15 percent of GDP in 2003 and in 2004, the external debt ratio would increase by 14 percentage points of GDP by 2005. Notwithstanding the relatively high volatility of the current account-to-GDP ratio in the past, these levels would be rather exceptional given that the highest current account deficit-to-GDP ratio was 17 percent in 1992.<sup>24</sup> A similar end-period outcome is generated by the combined interest rate, GDP growth and inflation, and current account shocks (Test 6). The impact of nominal interest rate shocks would be more limited (Test 2), with each additional 100 basis point increase (from 2003 to 04) adding about half a percentage point to the external debt ratio during the projection period.

10. By simply setting all the main macroeconomic variables at their historical values (Test 1), the external debt ratio would deteriorate steadily, reaching 78.5 percent in 2008 as compared with 67 percent in the baseline scenario. This outcome reflects that, with lower growth and larger external current account deficit at historical levels, the external debt dynamic would become explosive.

### III. CONCLUSION

11. The medium-term framework reflecting the current strategy of the authorities would leave external debt ratios at relatively high levels, while total government debt would decline steadily in line with the repayment of domestic arrears. The stress tests conducted above show that, in the absence of fiscal discipline, both government debt and external debt ratios would deteriorate and become unsustainable in the occurrence of adverse temporary economic shocks. Therefore, the sustainability of the medium-term framework hinges on

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<sup>24</sup> Also, a more significant current account deterioration is projected for 2007 and 2008.



the government's ability to maintain a solid macroeconomic situation through:  
(a) implementation of policies, which could enhance Djibouti's competitiveness and support higher economic growth; (b) continued fiscal consolidation and implementation of reforms (including simplifying the exemptions system and introducing a VAT); and (c) cautious external debt policies, including by maximizing foreign grants.

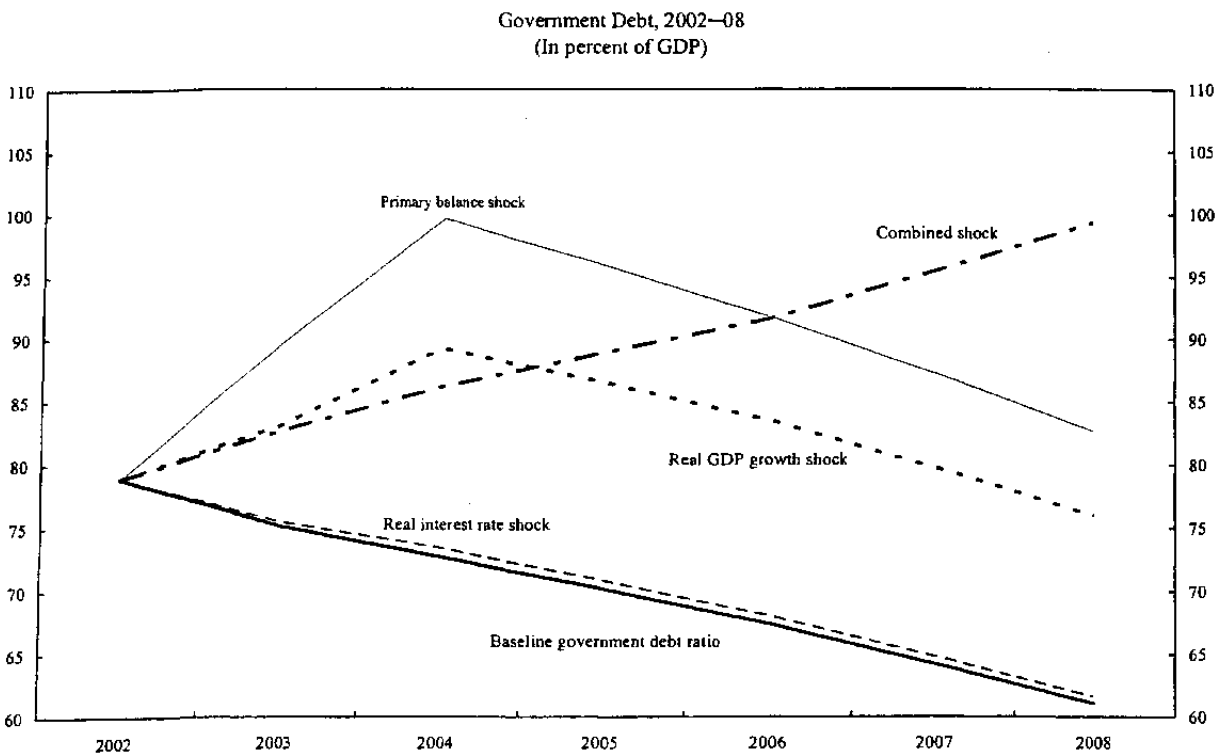
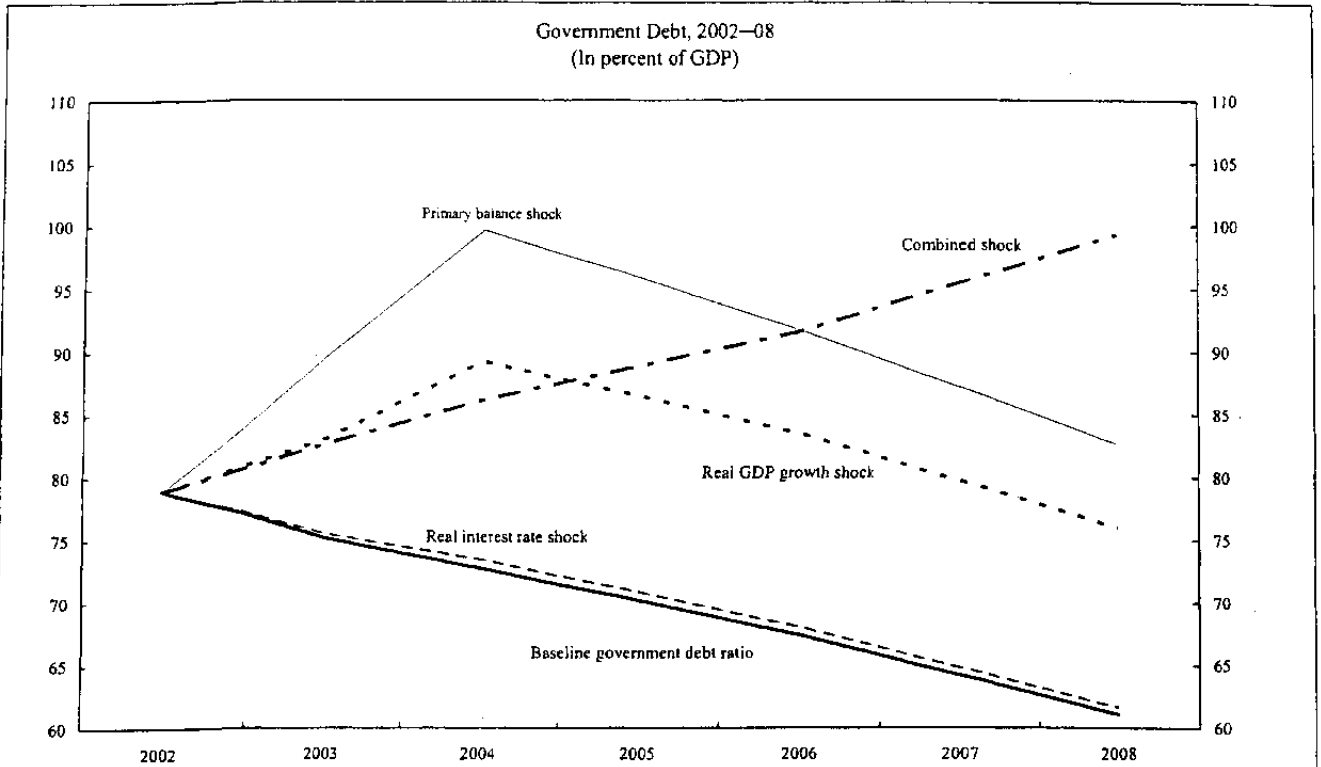


Table 1. Djibouti: Government Debt Sustainability Framework, 2002–08

(In percent of GDP; unless otherwise indicated)

	Projections						
	2002	2003	2004	2005	2006	2007	2008
<b>I. Baseline Medium-Term Projections</b>							
Government debt 1/ without foreign-currency denominated	78.9	75.2	72.8	70.2	67.4	64.2	61.1
Change in government debt	0.3	-3.7	-2.4	-2.6	-2.8	-3.2	-3.1
Identified debt-creating flows (4+7+12)	1.1	-2.8	-1.2	-0.6	-0.8	-2.3	-2.3
Primary deficit	3.3	0.5	2.4	2.6	2.7	1.5	1.7
Revenue and grants	29.4	34.5	33.7	33.4	31.5	32.0	31.3
Primary (noninterest) expenditure	32.7	35.0	35.8	36.0	34.3	33.5	33.0
Automatic debt dynamics 2/	-2.2	-3.3	-3.2	-3.2	-3.6	-3.8	-4.0
Contribution from interest rate/growth differential 3/	-2.2	-3.3	-3.2	-3.2	-3.6	-3.8	-4.0
<i>Of which</i>							
Contribution from real interest rate	-0.3	-1.0	-1.0	-1.0	-1.0	-0.9	-0.9
<i>Of which</i>							
Contribution from real GDP growth	-2.0	-2.3	-2.2	-2.2	-2.6	-2.8	-3.1
Contribution from exchange rate depreciation 4/	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other (specify, e.g., bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Residual, including asset changes (2-3)	-0.8	-1.0	-1.2	-2.0	-2.0	-0.9	-0.8
Government debt-to-revenue ratio 1/	268.2	217.6	215.9	210.3	213.8	200.7	195.0
Gross financing need 5/ In millions of U.S. dollars	4.0	1.7	3.4	3.8	3.9	2.6	2.8
	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Key Macroeconomic and Fiscal Assumptions</b>							
Real GDP growth (in percent)	2.6	3.0	3.1	3.2	3.9	4.5	5.2
Average nominal interest rate on government (in percent) 6/	0.3	0.7	0.7	0.7	0.6	0.6	0.6
Average real interest rate (nominal rate minus change in GDP deflator, in percent)	-0.3	-1.3	-1.3	-1.3	-1.4	-1.4	-1.4
Nominal appreciation (increase in U.S. dollar value of local currency, in percent)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Inflation rate (GDP deflator, in percent)	0.6	2.0	2.0	2.0	2.0	2.0	2.0
Growth of real primary spending (deflated by GDP deflator, in percent)	10.8	10.2	5.3	3.9	-1.1	2.0	3.7
<b>II. Stress Tests for Public Debt Ratio</b>							
Real GDP growth, real interest rate, and primary balance are at historical averages in 2003–07	78.9	82.7	86.2	88.9	91.6	95.4	99.3
Real interest rate is at historical average plus two standard deviations in 2003 and 2004	78.9	75.5	73.5	70.9	68.0	64.8	61.6

Table 1. Djibouti: Government Debt Sustainability Framework, 2002–08 (concluded)

(In percent of GDP; unless otherwise indicated)

	Projections						
	2002	2003	2004	2005	2006	2007	2008
Real GDP growth is at historical average minus two standard deviations in 2003 and 2004	78.9	83.1	89.2	86.5	83.5	79.8	76.0
Primary balance is at historical average minus two standard deviations in 2003 and 2004	78.9	89.7	99.6	95.9	91.8	87.2	82.7
Combination of 2–4 using one standard deviation shocks	78.9	90.3	101.7	92.8	84.1	75.2	66.6
One time 30 percent real depreciation in 2003 7/	78.9	96.6	93.3	89.9	86.1	81.8	77.6
10 percent of GDP increase in other debt-creating flows in 2003	78.9	85.2	82.3	79.3	76.1	72.4	68.8
Impact on debt-to-GDP ratio if revenue-to-GDP ratio is at historical average minus two standard deviations in 2003–04	78.9	84.1	89.4	86.1	82.5	78.5	74.5
Impact on debt-to-revenue ratio if revenue-to-GDP ratio is at historical average minus two standard deviations in 2003–04	268.2	328.6	349.5	258.1	261.8	245.3	237.8
<b>Historical Statistics for Key Variables (past 10 years)</b>	<b>Historical Average</b>	<b>Standard Deviation</b>	<b>Average 2002–08</b>				
Primary deficit	5.1	5.0	2.1				
Real GDP growth (in percent)	-1.1	2.8	3.6				
Nominal interest rate (in percent) 6/	0.8	0.3	0.6				
Real interest rate (in percent)	-1.6	0.4	-1.2				
Inflation rate (GDP deflator, in percent)	3.4	1.5	1.8				
Revenue to GDP ratio	33.5	4.0	32.3				

1/ Covers central government debt on a year basis.

2/ Derived as  $[(r - p(1+g) - g + ae(1+r))/(1+g+p+gp)]$  times previous period debt ratio, with  $r$  = interest rate;  $p$  = growth rate of GDP deflator;  $g$  = real GDP growth rate;  $a$  = share of foreign-currency denominated debt; and  $e$  = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).3/ The real interest rate contribution is derived from the denominator in footnote 2/ as  $r - \pi(1+g)$  and the real growth contribution as  $-g$ .4/ The exchange rate contribution is derived from the numerator in footnote 2/ as  $\alpha e(1+r)$ .

5/ Defined as government deficit, plus amortization of medium and long-term government debt, plus short-term debt at end of previous period.

6/ Derived as nominal interest expenditure divided by previous period debt stock.

7/ Real depreciation is defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

Table 2. Djibouti: External Debt Sustainability Framework, 2002–08

(In percent of GDP; unless otherwise indicated)

	Projections						
	2002	2003	2004	2005	2006	2007	2008
I. Baseline Medium-Term Projections							
<b>External debt</b>	<b>66.8</b>	<b>66.5</b>	<b>68.0</b>	<b>68.4</b>	<b>68.3</b>	<b>67.6</b>	<b>66.5</b>
Change in external debt	1.6	-0.3	1.4	0.5	-0.1	-0.7	-1.1
Identified external debt-creating flows (4+8+11)	3.3	0.0	2.3	2.2	0.6	0.8	0.2
Current account deficit, excluding interest payments	5.2	4.4	12.1	11.5	10.4	22.4	21.8
Deficit in balance of goods and services	14.8	18.7	24.9	25.3	22.8	35.7	34.9
Exports	46.1	48.8	49.0	49.0	48.6	47.4	46.8
Imports	60.9	67.5	73.9	74.3	71.4	83.1	81.7
Net non-debt creating capital inflows (negative)	-0.8	-2.1	-7.4	-6.8	-6.6	-18.0	-17.6
Net foreign direct investment, equity	0.8	2.1	7.4	6.8	6.6	18.0	17.6
Net portfolio investment, equity	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Automatic debt dynamics 1/	-1.1	-2.3	-2.4	-2.5	-3.1	-3.5	-4.1
Contribution from nominal interest rate	1.0	0.9	0.9	1.0	0.7	0.7	0.5
Contribution from real GDP growth	-1.7	-1.9	-2.0	-2.1	-2.5	-2.9	-3.3
Contribution from price and exchange rate changes 2/	-0.4	-1.3	-1.3	-1.3	-1.3	-1.3	-1.3
Residual, incl. change in gross foreign assets (2-3)	-1.7	-0.3	-0.9	-1.8	-0.8	-1.5	-1.3
External debt-to-exports ratio (in percent)	144.8	136.3	138.6	139.7	140.3	142.5	142.1
<b>Gross external financing need (in billions of U.S. dollars) 3/</b>	<b>0.0</b>	<b>0.0</b>	<b>0.1</b>	<b>0.1</b>	<b>0.1</b>	<b>0.2</b>	<b>0.2</b>
In percent of GDP	8.0	7.2	15.0	14.4	13.1	24.9	24.1
<b>Key Macroeconomic and External Assumptions</b>							
Real GDP growth (in percent)	2.6	3.0	3.1	3.2	3.9	4.5	5.2
Exchange rate appreciation (U.S. dollar currency) value of local currency, change in percent)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
GDP deflator in U.S. dollars (change percent)	0.6	2.0	2.0	2.0	2.0	2.0	2.0
Nominal external interest rate (in percent)	1.6	1.5	1.4	1.5	1.1	1.0	0.9
Growth of exports (U.S. dollar terms, in percent)	4.2	11.2	5.6	5.2	5.3	3.9	5.9
Growth of imports (U.S. dollar terms, in percent)	9.0	16.5	15.1	5.8	1.9	23.9	5.5

Table 2. Djibouti: External Debt Sustainability Framework, 2002–08 (concluded)

(In percent of GDP; unless otherwise indicated)

	Projections						
	2002	2003	2004	2005	2006	2007	2008
<b>II. Stress Tests for External Debt Ratio</b>							
Real GDP growth, nominal interest rate, dollar deflator, non-interest current account, and non-debt inflows are at historical average in 2003–08	66.8	69.6	71.8	73.1	75.3	76.8	78.4
Nominal interest rate is at historical average plus two standard deviations in 2003 and 2004	66.8	66.9	68.8	69.2	69.0	68.3	67.1
Real GDP growth is at historical average minus two standard deviations in 2003 and 2004	66.8	73.2	81.9	81.8	81.1	79.7	77.9
Change in U.S. dollar GDP deflator is at historical average minus two standard deviations in 2003 and 2004	66.8	67.6	70.1	70.4	70.2	69.4	68.2
Non-interest current account is at historical average minus two standard deviations in 2003 and 2004	66.8	77.0	80.8	80.8	80.1	78.8	77.0
Combination of 2–5 using one standard deviation shocks	66.8	76.6	80.8	80.8	80.1	78.8	77.0
One time 30 percent nominal depreciation in 2003	66.8	94.1	94.6	94.1	92.7	90.8	88.3
<b>External Debt Ratio (Alternative scenario)</b>	66.8	67.3	69.1	70.6	72.8	74.7	76.0
<b>Historical Statistics for Key Variables (past 10 years)</b>	<b>Historical Average</b>	<b>Standard Deviation</b>	<b>Average 2002–08</b>				
Current account deficit, excluding interest payments	4.7	5.1	12.5				
Net non-debt creating capital inflows	0.5	0.2	8.5				
Nominal external interest rate (in percent)	0.6	0.7	1.3				
Real GDP growth (in percent)	-1.1	2.8	3.7				
GDP deflator in U.S. dollars (change in percent)	3.4	1.5	1.8				

1/ Derived as  $[r - g - r(1+g) + ea(1+r)] / (1+g+r+gr)$  times previous period debt stock, with  $r$  = nominal effective interest rate on external debt;  $r$  = change in domestic GDP deflator in U.S. dollar terms,  $g$  = real GDP growth rate,  $e$  = nominal appreciation (increase in dollar value of domestic currency), and  $a$  = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as  $[-r(1+g) + ea(1+r)] / (1+g+r+gr)$  times previous period debt stock.  $r$  increases with an appreciating domestic currency ( $e > 0$ ) and rising inflation (based on GDP deflator).

3/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

**Statement by the IMF Staff Representative**  
**January 7, 2004**

1. This statement summarizes discussions on future Fund involvement in Djibouti, which were held during a staff visit in Djibouti from December 7–14, 2003, and after the staff report was circulated to the Executive Board on December 5, 2003. It does not change the thrust of the staff appraisal.
2. The staff explained to the authorities that a period of decisive policy implementation was required before possibly entering into a new arrangement under the Poverty Reduction and Growth Facility (PRGF). Moreover, the staff noted that, provided that donors continue to grant Djibouti nonmilitary budgetary aid in support of its economic reforms, there would not be a balance of payments financing need in 2004.
3. The authorities agreed with the staff's recommendation to move to a Staff Monitored Program (SMP), covering at least twelve months, to establish a strong track record of policy reform and mobilize adequate external financial assistance. Under this program, the authorities intend to complete the unfinished reform agenda of the previous PRGF arrangement, including measures to strengthen the fiscal position and increase competitiveness (such as privatization and adoption of new labor and investment codes). In addition, the program would include additional measures to improve governance and transparency (such as periodic publication of government accounts audit and reports on expenditures in priority social areas) and strengthen social safety nets.
4. It was agreed that the staff would return to Djibouti to finalize discussions on a SMP after two conditions are fulfilled: the adoption by the national assembly of a 2004 budget along the lines discussed with staff; and the transmittal by the authorities to the staff of a draft Memorandum of Economic and Financial Policies (MEFP) that clearly incorporates measures and a timetable to complete the unfinished reform agenda of the previous PRGF.
5. The 2004 budget was approved by the national assembly on December 29, 2003. The staff did not yet receive all the details of the approved budget in order to assess whether it fully reflects the latest discussions that were held during the December 2003 staff visit, including on achieving the objective of a 2.5 percent of GDP surplus in the domestic fiscal balance and the demobilization of 500 military at end-March 2004.



INTERNATIONAL MONETARY FUND

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March 19, 2004

International Monetary Fund  
700 19<sup>th</sup> Street, NW  
Washington, D. C. 20431 USA

## **IMF Concludes 2003 Article IV Consultation with Djibouti**

On January 7, 2004, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Djibouti.<sup>1</sup>

### **Background**

Macroeconomic performance in 2002 was mixed. After growing on average at about 1.3 percent per year from 1999–2001, real GDP grew by an estimated 2.6 percent in 2002—a level, however, that barely stabilized the continued decline of real GDP per capita observed during the last decade. This acceleration reflected an increase in government investment on social housing and buoyant port activities as Djibouti was able to attract additional transshipment activities. Consumer prices barely increased in 2002, maintaining the long-standing record of modest inflation in the country.

In the fiscal sector, following two years of steady improvement, the deficit widened. Despite higher revenues and grants, the overall fiscal deficit (payment order basis) increased to 3.5 percent of GDP from less than 2 percent in 2000–01. This deterioration reflected in particular a sharp increase in spending, notably goods and services and transfers. The authorities, however, managed to keep the wage bill—which accounts for almost half of current spending—under control in 2002 and further increased tax revenue by 0.6 percent of GDP to 21.1 percent—one of the highest levels in low-income countries. In addition, domestic arrears, in particular those associated with wage payments, were reduced. Meanwhile, broad money growth continued to be very strong in 2002 owing to higher net foreign assets of commercial

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<sup>1</sup> 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.



banks. In contrast, credit to the private sector declined for the third year in a row, as bank lending remained prudent amid an upward trend in nonperforming loans.

With imports associated with higher investments on the rise, the external current account deficit widened in 2002. Nonetheless, this deficit was more than offset by a surplus in the capital account resulting from higher external project financing and continued large unidentified capital inflows channeled through money changers. Despite the depreciation of the U.S. dollar, to which the Djibouti franc has been pegged at the same parity since the early 1970s, Djibouti's real effective exchange rate in mid-2003 remained 60 percent more appreciated than in 1980.

Limited progress was made in 2002 in advancing key structural reforms. The preparation of the 2000–01 financial accounts and intangible assets of the remaining public enterprises was completed in the second half of 2003. In addition, banking supervision has been strengthened. However, the long-overdue adoption of a revised labor code is still under discussion with labor unions, while the reform of the investment code and the accompanying streamlining and reduction of tax exemptions continue to be debated within the cabinet.

### **Executive Board Assessment**

Executive Directors noted that, following several years of financial adjustment efforts, Djibouti continues to face serious challenges. Poverty is pervasive and increasing, with high unemployment and large groups of the population lacking access to essential social services. Economic growth remains too low to contribute to an effective decline in poverty, and the economy remains highly dependent on the Djibouti port and its associated activities as well as on the foreign military presence.

Directors considered that macroeconomic performance and progress in implementing reforms during the last arrangement under the Poverty Reduction and Growth Facility were mixed. Despite the restoration of some degree of fiscal discipline, overall fiscal performance lagged well behind the program objectives, leaving very limited room for higher social expenditures. Although a number of—mainly fiscal—reforms were introduced, privatization and work on reforming the investment, labor, and commerce codes did not proceed as envisaged, while recent measures such as the establishment of three new public enterprises are an additional source of concern. Against the backdrop of the numerous slippages in policy implementation, Directors underscored the critical importance and urgency of putting in place a well-designed and realistic reform strategy, which the authorities will need to implement with strong ownership and determination. Technical assistance will play a crucial role in helping Djibouti strengthen its limited administrative capacity.

Putting economic growth on a higher and sustained path is a key challenge facing the authorities in the period ahead. Directors urged the authorities to support private sector development, in particular by increasing the pace and depth of reforms designed to strengthen Djibouti's external competitiveness. This will require a much more forceful and coherent implementation of the government's strategy of broad-based structural reforms and

maintenance of financial stability. Key priorities should be to reduce high labor costs, dismantle barriers to entry, and improve the regulatory environment for business and investment.

Directors expressed a wide range of views about the desirability of an action on the exchange rate to further improve Djibouti's external competitiveness. Some Directors considered that a carefully considered realignment of the exchange rate at an appropriate time should not be ruled out as one element of an overall policy package of structural reforms to restore external competitiveness. At the same time, Directors recognized that Djibouti's currency board arrangement has so far been a major source of stability within the economy, and that significant supportive policy steps—including prudent fiscal, monetary, and wage policies as well as the establishment of an appropriate safety net—would be required to accompany any action on the exchange rate. In light of this, and given the narrow production base of Djibouti's economy, a number of other Directors felt that the restoration of competitiveness would be better pursued through a focused and decisive effort to address the structural rigidities in the economy.

Directors considered that the large additional revenue from the foreign military now stationed in Djibouti should provide ample room for additional social expenditures and repayment of domestic debt. They regretted the large increase in nonessential expenditures in the revised 2003 budget, and urged the authorities to significantly alter allocations in favor of higher and well-targeted expenditures in priority sectors. In particular, the military demobilization program should proceed in order to allow a decline in the wage bill, usage of utilities should be much better controlled, and non-essential expenditures on goods and services should be reduced.

Directors encouraged the authorities to implement decisively the plan, prepared by the ministry of finance, to clear the stock of audited domestic budgetary arrears. They observed that repaying the arrears equitably and according to transparent priorities will greatly contribute to restoring the government's financial credibility.

Directors commended the authorities for the progress made in modernizing tax administration and strengthening the expenditure management process. Provided that further progress is made to integrate the functions of tax management, control, and collection, the tax administration reforms bode well for the introduction of a value added tax in early 2006 as currently planned. Directors encouraged the authorities to further enhance the transparency of public finances, in particular by publishing the reports of the public finance auditor's office and bringing all government accounts under the direct control of the ministry of finance's treasurer.

Directors saw the adoption of an anti-money laundering law and the beginning of an external audit of central bank accounts as encouraging steps toward protecting the integrity of Djibouti's financial system. They also welcomed the authorities' strategy to develop microfinance institutions. Priorities for the period ahead should be the adoption of the revised banking law and central bank statutes, the strengthening of the banking supervision capacity of the central bank, and more frequent inspections of financial institutions.

Directors urged the authorities to fully normalize their relations with donors and settle all remaining external arrears. They noted that recent improvements in the external debt database

should help strengthen external debt monitoring and avoid any new accumulation of external arrears.

To address statistical weaknesses, which continue to hamper policy analysis and monitoring, Directors encouraged the authorities to forcefully implement the recommendations of the various Fund technical assistance missions, and to consider participation in the Fund's General Data Dissemination System.

Directors considered that an effective and well-focused Fund staff-monitored program will provide an appropriate framework for assisting the authorities with the establishment of the needed track record of policy reform, in particular by completing the unfinished reform agenda of the previous PRGF arrangement. Such a program should lay the foundation for and be commensurate with an envisaged successor PRGF arrangement, building on efforts to strengthen institutional capacity and carefully taking into account the social impact of alternative reform scenarios.

**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 2003 Article IV Consultation with Djibouti is also available.

Djibouti: Selected Financial Economic Indicators, 1999–2003 1/

	1999	2000	2001	Est. 2002	Proj. 2003
<b>National income and prices</b>					
Real GDP (annual change in percent)	2.2	0.7	1.9	2.6	3.0
Consumer prices (annual average)	2.0	2.4	1.8	0.6	2.0
(In percent of GDP)					
<b>Consolidated government operations</b>					
Total revenue and grants 2/	30.9	31.0	28.2	29.4	34.5
Total expenditures	33.1	32.8	29.7	32.9	35.6
Overall balance (payment order basis)	-2.2	-1.8	-1.4	-3.5	-1.0
Change in arrears (decrease -)	1.3	0.5	-0.6	-0.7	-2.9
Overall balance (cash basis)	-0.8	-1.3	-2.0	-4.2	-3.9
Government domestic arrears (stock) 3/	29.3	29.6	28.9	27.8	24.9
(Change from proceeding December; in percent of broad money)					
<b>Money and credit</b>					
Broad money	5.2	1.1	7.5	15.7	5.1
Net foreign assets	5.7	-7.3	16.1	15.7	3.9
Net domestic assets	-0.5	8.4	-8.6	0.0	1.2
(In percent of GDP; unless otherwise indicated)					
<b>External sector</b>					
Current account	-0.6	-7.2	-4.3	-6.2	-5.3
Overall balance	1.5	-3.3	3.0	9.0	1.3
Official external debt after rescheduling 4/	62.8	66.9	65.2	66.8	66.5
Central bank gross foreign assets (in months of imports) 5/	3.2	2.9	3.2	3.1	2.8
<b>Exchange rate</b>					
Real effective exchange rate 6/ (end-year change in percent; depreciation -)	6.7	9.3	3.3	-8.4	-10.7

Sources: Djibouti authorities; and IMF staff estimates and projections.

1/ Based on official data as of November 2003.

2/ Starting 2003, includes the additional revenue from France and the United States.

3/ Domestic arrears include wage arrears and arrears to private and public suppliers for goods and services and pension funds.

4/ Public- and publicly-guaranteed debt of the central government and the public enterprise sector.

5/ Imports of goods for domestic use and nonfactor services.

6/ Data available through June 2003.