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MADAGASCAR ECONOMIC POLICY REFORM PROGRAM

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Abbreviations

AEPRP	-	African Economic Policy Reform Program
A.I.D.	-	Agency for International Development
CIP	-	Commodity Import Program
ESF	-	Economic Support Fund
FAA	-	Foreign Assistance Act
GDP	-	Gross Domestic Product
GDRM	-	Government of the Democratic Republic of Madagascar
IBRD	-	International Bank for Reconstruction and Development (World Bank)
IEE	-	Initial Environmental Examination
IMF	-	International Monetary Fund
IQC	-	Indefinite Quantity Contract
MARS	-	Madagascar Agriculture Rehabilitation Support project
MEPRP	-	Madagascar Economic Policy Reform Program
OGL	-	Open General Licensing System
OYB	-	Operational Year Budget
PAAD	-	Program Assistance Approval Document
PAIP	-	Program Assistance Identification Paper
PSC	-	Personal Services Contractor
REDSO	-	Regional Economic Development Services Office
RIL	-	Regime d'Importation Liberalise (Liberalized Import Regime)
SDAP	-	Social Dimensions of Adjustment Project
SDR	-	Special Drawing Rights
UNDP	-	United Nations Development Program
UNFPA	-	United Nations Family Planning Association
USDH	-	United States Direct Hire

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MADAGASCAR ECONOMIC POLICY REFORM PROGRAM

I. SUMMARY AND RECOMMENDATIONS

Since 1981, the Government of Madagascar has taken strong action to stabilize the economy of a country which remains one of the poorest in the world with a per capita GDP of US $265. Successfully complying with five successive IMF Standby Agreements, the Government of Madagascar has achieved substantial progress in cutting public expenditures, reducing the budget deficit, and slowing inflation. Measures have also been taken to restore market incentives, including a depreciation of the currency(by 48% from 1982 to 1985, with further substantial devaluations in 1986 and 1987), and a program of liberalization of prices and markets in the agricultural, industrial and transport sectors. In early 1987, the Government introduced a liberalized import regime(RIL) for raw materials, spare parts and consumer goods which by mid-year was expanded to include capital goods.

Despite these measures, economic growth so far has been negligible: after rising by 2% in 1984 and 1985, GDP grew by only 0.8% in 1986. The balance of payments has remained weak due to poor export performance and heavy debt service obligations, the latter estimated at 51% of exports after rescheduling in 1986. Most of the decline in exports can be attributed to pricing and marketing policies, although administrative constraints and external market conditions have also played a role. Imports have also fallen off by 50% in real terms since 1980, constrained not only by falling export receipts, but also by a substantial reduction in capital inflows. The reduction of imports has in turn adversely affected economic recovery by constraining agricultural and industrial output, as well as the operations of the transport sector.

The picture emerging from this review of performance is mixed: much progress has been made, yet in most areas this progress is fragile and in need of consolidation. As in any reform effort, the opposition of vested interests who benefit from the existing situation must be overcome. This is evident in the reform of the rice sector, where despite the rice buffer stock's success in stabilizing consumer prices and a good rice harvest in 1987, Government commitment to market liberalization appeared tentative in the fall of 1987. Population growth of 3% per year, and a rapidly eroding natural resource base constitute additional major barriers to long-term economic growth.

It is clear that significant new efforts will be required to move the Malagasy economy from a condition of stabilization to one of structural reform where real per capita growth can be

realized. Despite strong resistance from domestic elements which profit from the status quo, the Government at present sees no alternative to sticking with the reform program negotiated with the IMF and the World Bank. Plans for 1988 include:

- a substantial reform of the foreign exchange allocation system, in which the RIL will be replaced by an open general licensing system(OGL);
- a major reform of the financial sector, whereby private operators will be allowed to enter either in partnership with the public sector banks or independently;
- a more determined effort at the privatization and liquidation of inefficient parastatals in agriculture and industry;
- continued improvement in public sector budgeting through the establishment of program budgets in several key ministries and the inclusion of formerly off-budget items within the budget;
- liberalization of export marketing;
- development of a plan for investment and policy reform in the edible oil agricultural sub-sector.

Together these measures should move the Malagasy economy much further along in the transition to an economy responding to market forces rather than government directives.

The PAIP design team recommends that A.I.D. support the significant program of ongoing reforms in Madagascar through an African Economic Policy Reform Program(AEPRP) grant in FY 1988. AEPRP funds of $10 million will be combined with FY 1988 operational year budget(OYB) funds of up to $7 million for a first year funding level of $17 million, in what is seen as a three year effort. Years two and three will be funded from available OYB allocations in fiscal years 1989 and 1990.

The program for the first year is outlined in this document. Its main feature is a single cash transfer of $15 million to finance imports under the open general licensing system(OGL). This cash transfer will be conditioned on the putting in place of a liberalized import system; if the OGL is not introduced in the timeframe now proposed, the cash assistance could be tranched. In addition, approximately $2 million will be provided for training, short term technical assistance and studies to support the policy reform agenda which will be the centerpiece of the agreement between A.I.D. and the Government of Madagascar. The PAIP design team further recommends that a categorical exclusion be approved for the proposed AEPRP based on the justification provided in the initial environmental assessment found in Annex B.

In identifying a tentative agenda, the two main considerations were that A.I.D. should support the considerable reform programs already formulated by the IMF and the World Bank,

rather than take new departures, and secondly, that the agenda should build upon the ongoing A.I.D. program in Madagascar. The candidates for inclusion in the reform agenda are: deepening and/or broadening rice liberalization reforms, pursuing the relationship between population and development, preserving the natural resource base, and budget rationalization. These will be further explored during the PAAD design. In the second and third years of the program, the policy reform agenda will be refined in light of previous years' experience and incorporated in grant agreement amendments.

II. BACKGROUND*

A. Setting

1. Land and People

Madagascar, an island nation in the Indian Ocean with an area the size of Texas, is among the poorest countries in the world with a per capita income of US$265 in 1986. It is, however, a country well endowed with natural resources amid a surprising diversity of soils, ecology and climates which permit the production of a wide range of agricultural products. The least developed regions are the semi-arid zones of the south and southwest coast, which are characterized by infertile soils. The temperate central high plateau is the economically most advanced region. The humid tropical lowlands and rainforests of the east coast are rich agriculturally, yet suffer the ravages of periodic cyclones. The extensive plains of the western coast provide pastureland for a significant portion of the country's herd of ten million cattle, as well as some tropical agriculture. This ecological diversity, and the isolation of Madagascar resulting from an early separation from the African mainland, have led to the evolution of unique species of flora and fauna whose preservation is now a primary concern of conservationists. Madagascar is moderately rich in minerals, mostly unexploited, as well as a largely untapped network of rivers which offer great potential for irrigation and hydroelectric power.

With this great agro-ecological diversity, it is no surprise that agriculture is the mainstay of the Malagasy economy, accounting for 40% of GDP, 80% of export earnings, and employing nearly 85% of the population. Rice is the basis of the Malagasy diet and economy, and is produced by 70% of all

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* The information in this section is drawn primarily from the following two documents; 1. Madagascar Agricultural Sector Adjustment Operation, IBRD, April 1986, and 2. Madagascar Industry and Trade Policy Adjustment Program, IBRD, June 1987.

farmers. The major export crops are coffee, vanilla, cloves and pepper.

Of Indo-Malay and African origin, Madagascar's ten million people (1986 estimate) form a highly homogeneous population, despite a low population density of 17 per square kilometer and widely dispersed population centers. Growing at a rate estimated at 3.0 percent a year, Madagascar's population is outstripping advances in agricultural production and putting considerable pressure on the natural resource base.

2. Economic Trends

After growing at an average annual rate of about three percent in the decade following independence in 1960, based largely on the performance of the agricultural sector, the economy underwent significant changes following the 1972 and 1975 revolutions. The socialist regime which came to power in 1972 emphasized state control of the economy; it nationalized most of the larger private companies, established control over agricultural marketing, adopted interventionist practices, and introduced policies aimed at self-sufficiency in agriculture and industry. When the current regime came to power in 1975 it further extended these policies. The result was stagnating agricultural output, increasing food imports, and a declining per capita GDP growth rate from 1973-1978.

Following several frustrating years of low growth, the Government attempted in 1978 to reverse the economic decline through a large public investment program aimed at rapid industrialization to diversify the economy. This program relied heavily on external commercial borrowing. Unfortunately, many of the projects begun at this time proved to be financially and economically unviable, and thus made little contribution to gross domestic product, exports or debt servicing capacity.

By 1981, the Malagasy economy was in serious desequilibrium as a result of the large and inappropriate public investment program of 1978-81, the sharp deterioration in the country's terms of trade associated with the large increase in petroleum prices, and the government's insistence on maintaining a fixed exchange rate. The central government fiscal deficit, which had averaged 2.5 percent of GDP between 1970 and 1978, reached 18 percent of GDP in 1980. Of this, approximately half was financed through the domestic banking system. As a result, inflation (measured by the urban consumer price index for traditional households) reached 30 percent in 1980 and the balance of payments deteriorated sharply. The resulting decline in import capacity and the stagnation of exports produced a decline in GDP of almost 10 percent in 1980. The Government initially responded to the balance of payments

deficit by tightening import controls which led to further declines in input availability and production.

By 1982, real GDP per capita had fallen by 28 percent from its 1973 peak, external debt service obligations had increased from 4 percent of exports of goods and non-factors services in 1978 to 72 percent in 1982. As a result of a fixed exchange rate and accelerating domestic inflation, the real effective exchange rate peaked at almost 40 percent above its 1978 level in mid-1983.

II. B. Macroeconomic Reforms to Date

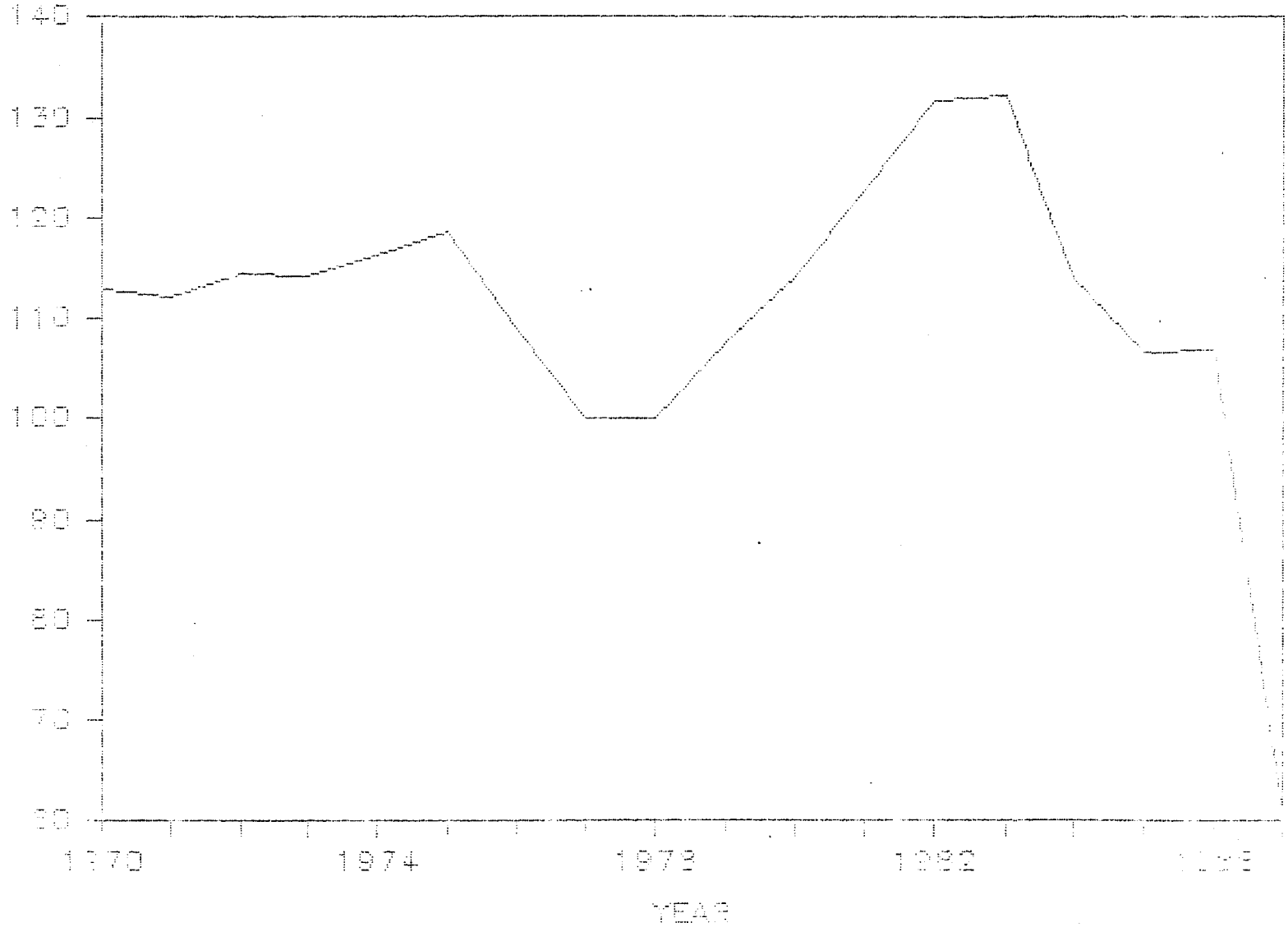
Beginning in 1982, the government began to take strong stabilization measures to restore equilibrium to the Malagasy economy. These efforts were undertaken in conjunction with the IMF and the World Bank. The Government has since met the conditions on five Standby Agreements with the IMF, and has been so successful in improving aggregate demand management and exchange rate adjustment that the IMF approved a Structural Adjustment Facility Arrangement in September of 1987. The Government of Madagascar has also received assistance from the World Bank for several sector specific adjustment programs, industry(1985), agriculture(1986) and trade(1987) involving major deregulation and liberalization of agricultural, ex-factory, and retail transactions.

As a result of these stabilization measures, government capital expenditures were reduced from 11.6 percent of GDP in 1981 to 7.5 percent in 1982 and approximately the same level in subsequent years. Of this, approximately two-thirds was externally financed. In addition, central government current expenditures were steadily reduced from 16.7 percent of GDP in 1981 to 12.9 percent of GDP in 1983, despite a steadily rising burden of interest on external debt. Overall, the central government deficit, measured on a cash basis, was reduced to 14.9 percent of GDP in 1981, 8.8 percent in 1982, 6.7 percent in 1983, and 4.0 percent in 1986. The portion of this financed through the domestic banking system was reduced from 7.4 percent of GDP in 1981 to only 1.3 percent by 1985. Unfortunately, progress in reducing the deficits of the parastatals was less uniform.

The government was somewhat slower to adjust the exchange rate. Although the government had begun to adjust the nominal exchange rate as early as mid-1980, the initial adjustments were inadequate to offset accelerating inflationary pressures and the real effective exchange peaked in mid-1983. Continuing adjustment and decelerating inflationary pressures produced significant exchange rate adjustment in the second half of 1986. After another large adjustment in June 1987, the real effective exchange rate as of mid-1987 stood at less than half its value of 1978 (see graph next page).

FIG. 1: REAL TRADE-WEIGHTED X-RATE

MADAGASCAR



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II. C. Sectoral and Structural Reforms to Date

1. Exchange Market Liberalization. Despite the significant adjustments of the exchange rate, foreign exchange continued to be allocated by a cumbersome administrative process through the end of 1986. At the beginning of 1987, the government instituted a "liberalized import regime" (RIL) for the importation of raw materials, spare parts, and consumer goods, excluding those financed by donors. The initial application of the RIL eliminated the element of discretion for about 25 percent of the total import bill. Under the RIL, importers would apply for a fixed amount of foreign exchange and pay a non-refundable deposit equal to 10 percent of the requested amount. The amount available would be divided by the total value of applications and each applicant would receive that percentage of his original request. The effective exchange rate (including the non-refundable fee) would thus rise in the face of excess demand for foreign exchange.

The initial use of the RIL was highly controversial and importers complained about the uncertainty both as to the amount of foreign exchange they would receive and the amount they would pay for it. In July 1987, the RIL was extensively modified as part of the government's Industry and Trade Policy Adjustment program with the World Bank. The non-refundable premium was reduced from 10 to 5 percent of the requested allocation. Financial support to the RIL was increased from the previous SDR 7 million per month to SDR 12 million; the separate allocations for raw materials and spare parts and for consumer goods were unified, while capital goods purchases were included under the system; and 80 percent of the categories of imports were freed from controls.

Although it is a significant improvement over the previous system of administrative allocation, the RIL is a highly imperfect substitute for a market clearing system of exchange allocation. The government has committed itself to instituting in 1988 a system of "Open General Licencing" (OGL) in which all importers would have essentially unlimited access to foreign exchange at a fixed rate. The remaining unresolved questions concern the timing of this change and whether the OGL is to be implemented all at once or in stages.

2. Rice Market Liberalization. By far the most thoroughgoing and most controversial of the reform measures taken to date has been the liberalization of the

commercialization of rice. Prior to May 1983, the Government had an absolute monopoly of the purchase and sale of rice. In 1982, the retail price of rice was raised 82 percent, eliminating the explicit consumer subsidy and improving producer prices. In 1983, a government decree specified that there was to be free competition in rice marketing except in two specific geographic areas which accounted for 25 percent of rice production. In the same year, quantity restrictions were placed on imports. In June 1985, the legally established ceiling price for rice was abolished.

As a result of these measures, regional price differences fell substantially, many new traders entered the rice market, rice millers created new distribution networks, state trading companies broadened their participation in wholesale trade, and many small mills came into the market (90 were authorized in 1985 compared with 11 in 1983).

However, the initial production response to the measures was disappointing. As part of its 1986 Agricultural Sector Adjustment Operation, therefore, the government agreed to more far reaching measures. In April 1986, the two remaining regional monopsonies were eliminated. In addition, the government sharply curtailed below market price official rice distributions and announced the elimination of such operations altogether in April 1987. To prevent unacceptable price rises in times of shortage, the government established a "buffer stock" with donated rice, the operation of which would be governed by a retail-level trigger price. This is not a true buffer stock since the government does not buy when prices are low, but rather a reserve to prevent shortages and politically unacceptable rises in consumer prices. For the 1986-87 season, the agreed trigger price was set at 40 percent above the average market price during the post harvest period.

The operation of this mechanism has been less than fully satisfactory. The institution of the buffer stock succeeded in holding consumer prices in 1986-87 within agreed limits. This was followed, however, by a sharp drop in retail and farm-gate prices after the 1986-87 harvest. In part this was due to the exceptionally good harvest of 1986-87, yet it also combined with larger than needed imports of rice from abroad and remaining stocks from the preceding harvest to lead to a very large overhang of government-held rice. The resulting producer price uncertainty, unless resolved, may prove to be a serious disincentive to production in 1988.

An additional problem appears to be the persistence of local government intervention in rice transportation and marketing. Nonetheless, the evidence of a smoothing out of regional price differentials suggests that effective market mechanisms have emerged as a result of the liberalization.

3. Transport liberalization. Because of its rugged topography and the long distances between the principal cities, and between major agricultural areas and principal cities, Madagascar suffers from certain inherent difficulties with regard to transportation. In the past, these difficulties have been compounded by extensive and ill-conceived government intervention in the sector. The national government intervened extensively in road transport by restricting routes, setting tariffs, controlling entry, and imposing selective controls on commodity movements. In addition, local authorities could and did tax road transport and impose both systematic and ad hoc restrictions on the movement of commodities.

During the course of 1987, the government eliminated restrictions on transport sector entry and transport price controls, although local taxation and regulation remain problems.

4. Price Liberalization. Beginning in the late 1970s, the government introduced a comprehensive system of price controls at each stage of the production and marketing process. This was in addition to the government monopoly of the marketing of agricultural products which existed until 1982. In 1982, the government began the process of decontrol of prices by streamlining the process by which price controls could be adjusted. In 1985 and early 1986, ex-factory price controls were eliminated for all but 31 manufactured goods. In August 1986, controls were lifted on 21 of these goods, leaving 10 products, accounting for 8 percent of manufacturing value added, subject to control.

Controls on retailing margins have been liberalized more slowly. However, margin controls on all but 16 products were removed in April 1987, and the government is committed under the terms of the Industry and Trade Policy Adjustment Program with the World Bank to eliminate the remaining controls by 1988 in two stages.

5. Financial Market Liberalization. The Government of Madagascar, until very recently, has been extremely

reluctant to consider significant moves to liberalize the financial sector. Following the nationalization of private banks in the mid-1970s, these institutions were reorganized along sectoral lines into three institutions which, until recently, shared a common board of directors. These institutions proceeded to lend large amounts of capital to parastatals. As a consequence, about 50 percent of the outstanding portfolio of the banks is non-performing. The only liberalization move which the government has been willing to take to date has been to decontrol most interest rates. Within the context of a nationalized banking system, this has had the effect of allowing the state banks to collect monopoly rents which are, in effect, transferred in a non-transparent subsidy to the parastatal sector. The present spread between deposit and lending interest rates is about 10 percent.

Significant moves to liberalize the financial sector are thus difficult to separate from the knotty problem of the financially troubled parastatals. Any moves to open the financial sector to private sector competition would undoubtedly force down the spread which the state banks are currently earning, forcing the government to absorb directly the unrecognized losses of the banking system through one mechanism or another, over a short period of time. This could have troublesome monetary consequences.

II. D. Remaining Problem Areas

The Government of Madagascar is committed to moving far along the road to a fundamental restructuring of the economy, from one in which fundamental decisions about resource allocation are made by the state to one in which such decisions are made by autonomous economic actors responding to market forces. Clearly much remains to be done. Principal agricultural exports are controlled by export monopolies exercising an onerous degree of implicit taxation. Production of major export crops continues to decline as real producer prices remain at half their 1979 levels and the relative prices of food crops go up. The state monopoly of the financial sector is preoccupied with the financial problems of the parastatals and provides a spotty level of service to the private sector at very high cost. The continuing presence of about 155 parastatals in key industries is a potentially serious problem both from an efficiency point of view and because of the continuing financial difficulties of these enterprises.

A major long-term problem is the nature of government's budgeting process which is fragmented, static, and does not

facilitate the systematic consideration of competing resource uses. Despite the success which the Government has had in improving its fiscal performance, the resources available to the public sector remain extremely scarce and will continue to be scarce for the foreseeable future. In this context, it is essential that the government develop procedures which permit a systematic and comprehensive consideration of competing demands on resources available to the public sector. This process must include:

a) a budget which reflects all resources available to, as well as all expenditures by, the public sector. At the present time, some donor financed activities, most counterpart generated by donor financing, and the transfers to the Treasury and subsequent expenditure of the receipts of the Caisses de Stabilisation (the government export monopolies) are not reflected in the budget;

b) a budget which is revised in light of changing conditions and priorities;

c) investment activities that are approved only after systematic appraisal, including consideration of alternative activities;

d) the comparison of actual expenditures with budget provisions at the end of each year and not after a lag of several years as is now the case;

e) government subsidies to parastatals explicitly reflected in the budget process; and

f) the compilation of government arrears, and payments to be made against them included in the budgeting process.

Clearly, the problem of export incentives for traditional agricultural exports (coffee, vanilla, cloves and pepper) must be addressed, consistent with the needs of the government for tax revenue, and consistent with the probable future reimposition of coffee quotas and Madagascar's position as the world's principal producer of vanilla.

Although the government's performance in the area of economic policy has been impressive, it has been less energetic in dealing with the critical social areas of population policy and the protection of the environment, especially the preservation of Madagascar's unique animal and plant species.

In the area of population policy, the government still has no explicit policy on child spacing. A 1920 law forbidding the sale of contraceptives remains on the statute books, even though it is not enforced.

The most important immediate reform, however, appears to be the continued liberalization of the exchange regime so that essentially all foreign exchange uses are allocated by a free market at a market clearing exchange rate.

Beyond that, virtually all of the reform measures undertaken to date require follow up. The policy distortions which are being dismantled in Madagascar did not happen by accident. They were put in place over a period of years because groups within the economy found the distortions advantageous. Although the present government sees the benefits of implementing policies which improve the general welfare, particular interests will certainly remain powerful and the danger exists that policy distortions will reappear under slightly different guises. We are joining a process of policy reform which is sure to extend over several years and in which there will certainly be setbacks. The present government has made a very promising start and it is expected that the ongoing process of policy dialogue and support will be fruitful.

II. E. A.I.D. Program in Madagascar

The major objective of the on-going A.I.D. program in Madagascar is to help the country achieve and maintain food self-reliance, particularly in rice, in ways that are consistent with the conservation of the natural resource base. The CDSS adopted in 1986 outlines five sets of actions that are to be taken to achieve that objective.

1. Continuing policy dialogue, through annual in-country agriculture policy workshops following upon study tours for key policymakers, and through the services of a leading U.S. economist.

2. Agriculture production response, by assisting in the introduction of improved rice varieties and technologies, productive infrastructure rehabilitation, soil conservation, and imports of key farm and marketing commodities.

3. Food Interventions, aimed at curtailing price rises which occur under conditions of scarcity while agricultural policy reforms undertaken by the government to stimulate domestic production are implemented (rice buffer stock program, proposed PL 480 Title II Section 206 edible oil program).

4. Private Sector Involvement, in part through studies aimed at improving the delivery of goods and services to the small farmer, as well as by counterpart fund credits, and a commodity import program.

5. Population and Family Health, through a combination of technical assistance and commodities which aim at increasing the availability of family planning services, and perhaps more importantly, at assisting the Government to frame and launch a national population and development program.

Until 1987, these actions have been undertaken through a short-term exploratory program consisting of PL 480 programs(Title I and II and Food for Progress), one bilateral project activity(Madagascar Agriculture Rehabilitation Support), a grant to the International Rice Research Institute, and centrally funded population and bio-diversity grant programs. In May 1987, a decision was made to establish the Madagascar program on a longer term basis. To that end, a Program Review Team was formed which from October 30- November 17, 1987 carried out a thorough assessment of the Madagascar program .

The main conclusion of the assessment team was that the A.I.D. strategy and program objective continues to be valid, but that a tighter focussing of program activities is desirable. The team recommended that increased A.I.D. attention be given to the policy reform process through the design of an AEPRP program which would support the introduction of an open general licensing system (OGL) for imports and, with resulting counterpart funds, the budget reform process. This should be accompanied by the assignment of a direct hire program economist to Madagascar. The review team also recommended that the grant to IRRI should be extended to continue its highly promising rice research program. This should be accompanied by the recruitment of a personal services contractor(PSC) who combines expertise in agriculture and the environment.

Concerning the food aid program, the assessment team recommended that A.I.D. should hold in abeyance the second tranche of the Food for Progress Program until 1988 harvest estimates give an indication of need, but should move forward with the development of a Section 206 program in vegetable oil linked to policy reform in the edible oils sector. The final recommendation was that A.I.D. should continue its efforts in the population sector, but should consider seriously a separation of activities in the environment sector, in which A.I.D., while supporting PVO efforts aimed at natural resource conservation, would give special encouragement to private sector support for the preservation of Madagascar's unique biological diversity.

III. ECONOMIC POLICY REFORM AGENDA

A. Introduction

In keeping with the recommendations of the October-November, 1987 Program Assessment, the PAIP team explored a reform agenda for A.I.D.'s program which meets two important, although not unrelated criteria. First, consistent with past A.I.D. programming principles in Madagascar, the agenda supports the

World Bank's overall structural adjustment and sectoral reform programs rather than selecting new reform areas. Thus, by and large, we propose pursuing with the Government issues such as foreign exchange liberalization and budget rationalization where the groundwork has already been laid by the World Bank and the IMF. Second, every effort has been made to identify a preliminary reform agenda which is a logical follow-on to the current A.I.D. program. Hence, deepening and/or broadening rice marketing liberalization, as well as population and natural resource conservation, are areas which will be considered further, at the PAAD development stage, for inclusion in the A.I.D. reform agenda.

B. Foreign Exchange Liberalization

The government of Madagascar has recently entered into an agreement with both the World Bank and the IMF to move from the present interim "RIL" system described previously to an "Open General License" (OGL) system. A.I.D. has been informed by the government that its present plan is to make the transition in three stages, beginning on February 1, 1988 and achieving full implementation on July 1, 1988. In the first stage which will begin in February, inputs and raw materials will be imported under the OGL. In April, spare parts and capital goods will be brought under the new system, and finally, in July, the transition will be completed with the addition of consumer goods to the OGL. The OGL will represent a major final step in the transition toward a foreign exchange system governed by market demand rather than government fiat. Under the present system (the RIL), foreign exchange is freely available to all importers on an essentially equal basis. However, both the quantity made available and its price are determined administratively and any shortfall is rationed proportionally among purchasers. Under the OGL, the monetary authorities will undertake to supply foreign exchange to all importers at the prevailing price. The authorities will set a target level of foreign exchange reserves, and will adjust the exchange rate if reserves fall below that level. Thus, market demand, at each level of the real exchange rate, will determine both the price of foreign exchange and its distribution among prospective users.

C. Budget Rationalization

The current budgetary challenge facing Madagascar is to increase the allocative and economic efficiency of budget expenditures. This requires that the government undertake steps to ensure that the allocation of all resources across sectors support the nation's overall development goals, and that the use of funds within each sector is both efficient and

consistent with these overall objectives. The requisite actions to achieve the changes constitute a budgetary reform program which is responsive, over both the short and long term, to the evolution of political and economic development objectives of the country. Thus, to be most effective, the reforms must be both iterative, in order to take account of both changing governmental priorities and its perceptions of those priorities, and comprehensive, taking into account all the resources available to the Government.

The government has begun reforming its budgeting procedures and its budgetary programming processes. To date, the reforms undertaken have been within the Ministry of Agricultural Production and Agrarian Reform(MPARA), and the Ministry of Public Works, with planned expansion in the next phase to the Ministries of Health and Primary and Secondary Education. The reforms represent a logical extension of the government's recent fiscal austerity; after austerity, planning and programming procedures and perhaps a restructuring of budgetary expenditure within and among ministries are required in order to increase the efficiency, and developmental impact, of government's limited resources.

At the present time, the government's budget estimates are prepared annually, with documents covering the essential aspects of recurrent and investment activities. In addition, most revenues appear within the budget documents. Beyond the preparation of the estimates, the government does not appear to prepare supplemental estimates which reflect expenditure adjustments within a particular budget cycle. This is in part a result of a difference in approach to the use of a budget between a control and a planning document. In addition, a number of activities, relevant both to revenues and to expenditures, remain off-budget. These activities include many donor financed projects on the one hand, and the proceeds accruing to the Caisses de Stabilisation from export crops on the other. One important concern at this point is that off-budget activities be brought on-budget in order that the government have a clear and comprehensive picture of its development resources and expenditures.

In addition to the budget estimates themselves, the government prepares a document which accounts for actual expenditures which can be compared with the original estimates. Unfortunately, the government is not able to prepare these documents in a timely fashion; the most recent document was completed earlier this year for the 1979 budget cycle. This implies that the government is unable to know in a timely and accurate manner what actual, as contrasted with estimated, expenditures have been. This in turn makes it difficult for the government to judge the absorptive capacity of a particular sector, or the profitability of specific investments.

Finally, while the government considers ways to move ahead and consolidate its revenue and expenditure accounts, it is also embarking on a program designed to increase allocative efficiency among government investments. This program is called the Public Investment Program (PIP) which consists of an annual expenditure plan prepared by the government's Central Planning Directorate. The purpose of this document is to help the government implement policy choices regarding future expenditures. The work of the Central Planning Directorate also carries over into the development plans, the most recent of which has called for a restructuring of government expenditures. Current expenditure plans call for continued rehabilitation of existing infra-structure, increasing allocations to productive agricultural projects (to receive two-thirds of all allocations), and further rehabilitation and support to internal transport infrastructure.

The principal reforms which the government is currently reviewing include:

- steps to allow the government to undertake effective sectoral expenditure policies;
- passage of a consolidated budget which integrates all the operations covered by the General Treasury Operations;
- formulation of a three year rolling budget for the Public Investment Program; and
- consideration of program budgeting techniques, and expenditure efficiency criteria, which allow continuous review and reformulation of expenditures to support development strategies for the principal economic and social sectors. The government has begun to implement these reforms on a sectoral basis.

Reforms which have begun should be supported within Agriculture and Public Works and extended to other Ministries. In general, planning and programming remain weak, and coordination of expenditures still a rarity. Complete rationalization of budgetary allocations also requires that the government have a clear picture of its total resources and expenditures. This in turn argues for bringing on-budget those activities and accounts which are currently off-budget.

Issues and Opportunities

There are a variety of issues to be addressed with respect to this reform agenda. Examples include the speed and extent to which the reforms will be supported and extended; which parastatal expenditures and activities would be brought on-budget; and the extent to which all donor counterpart should be brought on-budget as revenue and donor financed projects as expenditures. The opportunity exists to support the preliminary reforms undertaken in the Ministries of Agriculture and Public Works, and the plans being made to extend these reforms to the Ministry of Health. In addition, support can be

provided to the Ministry of Finance to assist its evaluation and control functions, and to the Directorate of Central Planning to strengthen its capacity to select efficient project activities and sectoral allocations.

III. D. Other Reform Issues

1. Deepen/Broaden Agricultural Liberalization

a. Export Marketing and Prices

Export marketing remains heavily government-controlled, particularly for the traditional crops of coffee, vanilla, cloves and pepper which have been reserved for parastatal marketing companies. These crops are subject to a stabilization "Caisse" system, which suffers from poor administrative and financial management, excessive centralization of decision-making, and weak commercial practices.

Reform of export marketing, which is key to the stimulation of export crop production, hinges on the lightening of cumbersome administrative procedures and the elimination of government control over the major export crops. Moves in these directions were begun cautiously in 1986, when the government initiated a study to analyse the impact of present practices and recommend corrective actions consistent with sound economic management. The results of this study are expected to be available in February of 1988. Given the seemingly sacrosanct character of the Caisse System, the GDRM decision during the November 1987 IMF visit to liberalize the marketing of pepper and cloves in early CY 1988 was unexpected. This decision should greatly accelerate the reform process in export marketing, although the equally serious issue of administrative procedures remains to be addressed.

Needed reform on the export price side would appear to be of two types; 1) the elimination of the Caisse system and its replacement by ad valorem taxes as appropriate, and 2) the introduction of measures to stimulate export crop production, primarily by permitting producer prices to rise toward world market levels.

b. Rice Sector Liberalization

The successes to date of the rice sector liberalization and the establishment of a buffer stock have been described earlier. It has become increasingly evident in recent months, however, that this progress is fragile and that the Government of Madagascar's commitment to the reform process is tenuous.

The establishment of a buffer stock was in large part the result of a deep-rooted suspicion of the market which is prevalent in Madagascar. This suspicion, and lack of confidence in the buffer stock mechanism, led the Government of Madagascar to continue a high level of imports even when it was apparent that they would not be needed, and to use the parastatals to hold substantial stocks of rice throughout 1986 and into 1987 at high cost as a further government reserve.

Resistance to the liberalization measures can be found at several levels. At the highest political level there is concern that prices to the consumer are too high (especially as an election year begins), and there is tremendous pressure to keep prices below the level at which the buffer stock would operate. Despite an agreement with the World Bank, the GDRM has not announced that the buffer stock will operate in 1987/88 or at what intervention price.

At the level of the government enterprises, the two parastatals which previously enjoyed monopolies in the two major rice surplus areas - SOMALAC and FIFABE - have taken actions to preserve their predominent positions in the market by putting pressure on producers: in the case of SOMALAC, by offering a discount on farm inputs and equipment and guaranteeing peasants rice during the hungry period equal to 10 % of his/her sales; and in the case of FIFABE, by denying irrigation water to producers who sold to other buyers and by acting in concert with local authorities to prevent such sales.

At the local level, authorities have in some cases intervened to keep traders from selling rice at retail prices above the former official mark-up levels despite the abolition of price controls; have limited the number of required cards issued to rice collectors despite the legal free trade in rice; and have in some cases required that approved traders maintain a stock in the locality. It is perhaps at this level that the most difficult changes have yet to be effected. Local authorities have traditional obligations to assure local food security, and often obtain a substantial proportion of revenues from taxes on rice sales and processing. Informal roadblocks persist, and papers are required to move rice between regions. It has been jokingly estimated that each roadblock adds FMG 20 to the price of a kilo of rice, and although the actual costs of such interventions are not known, they are substantial. The prerogatives of local governments are enshrined in the Malagasy constitution, and exist alongside other legislation which is often contradictory. A World Bank study of local government revenue collection policies and procedures is now underway which is expected to make recommendations on alternative sources of revenue.

It is clear that there is considerable scope for the broadening and deepening of reform in the rice sector. To summarize the areas where further work is needed:

1) strengthening the understanding of and intellectual commitment to the liberalization process, particularly within the government administration and Parliament;
2) dismantling regulations which inhibit the free movement of rice, particularly at the local level;
3) finding alternative sources of revenue for local governments besides taxes on rice sales and movement;
4) assuring adequate supplies of credit to enable buyers to purchase rice from producers at harvest time;
5) assuring that government complies with commitments made in the buffer stock program;
6) divesting the marketing functions of the rice parastatals.

A.I.D. will begin to address the final point through the parastatal divestiture component of the Madagascar Agriculture Rehabilitation Support project, in response to an anticipated government request to prepare an action plan for disengaging the marketing service of SOMALAC.

C. Oilseeds sector

The oilseeds sector is one of key interest because of the importance of edible oils in a nutritionally balanced diet in a country where malnutrition is widespread, and because domestic production of edible oils has declined sharply in recent years, necessitating the import of nearly the entire domestic requirement. In the face of continuing shortages and low official prices, edible oils can be purchased often only on the black market and at prices beyond the reach of most consumers. The decline in production of oilseed crops can be attributed to far-reaching price and marketing controls introduced by the Government in the mid 1970's. Measures have since been taken to remove restrictions on marketing and to raise prices (first at the wholesale and retail levels, and in September 1987 at the ex-factory level, where prices were decontrolled), yet these measures have not had a significant impact on production. The Ministry of Commerce's Supply Office continues to exercise a pervasive control over distribution despite announced liberalization measures. This issue will be studied in the development of Section 206 conditionality.

A further complicating factor is the role of large parastatal oil refineries which dominate domestic production and marketing. These companies have significant unutilized capacity and operate at a loss. The economic viability of past and planned government investments in the oil seed sector needs to be reassessed.

A comprehensive study of the oilseeds sector recently completed with UNDP financing, failed to address the critical question of Madagascar's comparative advantage among the many oilseed crops being grown (groundnuts, soybeans and cottonseeds as well as oil palm and coconut), or to outline a rational program for the rehabilitation of the sector. The preparation and acceptance of a Master Plan for the sector, which will establish specific targets and interventions as well as outline the schedule for actions, is a condition for disbursement under the second tranche of the World Bank Agricultural Sector Credit.

A specific program for the reform of the sector has thus not yet been established, although it clearly would include a rationalization of investments in the sector based on comparative advantage, the divestiture or liquidation of poorly performing parastatal companies, and the cessation of government intervention on the marketing and distribution side, in part through a redefinition of the Ministry of Commerce's role in distribution.

Given the strong interest of several of the donors in the sector, a carefully coordinated multi-donor effort is required. A.I.D. has been the principal supplier of edible oil through the PL480 program, and A.I.D./Madagascar has proposed the replacement in FY 1988 of the Title I program with a multi-year 206 grant program which will be tied to a multi-donor supported reform package. This Section 206 program will be developed in March of 1988 if approval is received for utilization of Section 206 resources.

III. D. 2. Other Reform Issues: Population

The population issue has, until recently, remained both sensitive and controversial, and the Government still has no official population policy. As a result, despite the donor community's concern over the effect of increasing population pressure on Madagascar's resources and its prospects for economic growth, the donors have not yet attempted to confront the problem head-on.

In 1985, A.I.D. undertook a population and family health assessment which called for a phased, multi-year effort drawing on various centrally-funded programs to initiate a variety of activities, including (in the Government's order of priority):

(1) Strengthening family health service delivery within the Ministry of Health by orienting practitioners to the health benefits of child spacing;

(2) conducting a national seminar on population and development (held in April 1987 under the aegis of the Central Planning Directorate with a RAPID presentation to policy-makers), whose purpose was to initiate the process for developing the national population policy and to begin the process of integrating population into development planning;

(3) providing technical assistance in the collection and analysis of demographic statistics and research;

(4) supporting private and parastatal organizations which provide child-spacing services; and

(5) assisting the Ministry of Health in designing an information, education and communication(IEC) program on child spacing in its family health service program.

Since the 1985 assessment, A.I.D. efforts in population have been rounded out to include assistance to the planning and implementation of a national population census in 1990, for which the U.S. Bureau of the Census is providing technical assistance and training and for which A.I.D. is prepared to provide counterpart funds to cover local costs. A.I.D. will also provide counterpart funds to finance the local costs of a five year expanded immunization program for mothers and infants which will be initiated under UNICEF auspices.

The Government's acceptance of A.I.D.'s strategy for introducing population activities in Madagascar, stemming in part from the agreement on priorities reached by the working group at the April 1987 national seminar, suggests an emerging recognition of the population problem. Today, for example, the Government tolerates the provision of child spacing services by private organizations, including parastatals, even though a 1920 law prohibiting the sale of contraceptives remains in force. The World Bank capitalized on this nascent interest by flagging the population issue in its November 1987 structural adjustment program document as one which required future attention. Also, the Madagascar Policy Framework Paper (1987-90) calls on the Government to establish, at the highest national level, a multi-sectoral task force on population issues leading to the formulation of a population policy aimed at reducing the birth rate.

Donor attention on the population issue per se may now be overtaken somewhat by an apparent growing concern about the social impact of the structural adjustment process. During recent reviews of the structural adjustment program, the Directors of the World Bank emphasized that Madagascar and the donor community should step up efforts to soften the impact of economic adjustment on the poorest and most vulnerable groups of society. In the short run, this would involve undertaking measures to enhance food security, presumably through targetted feeding programs, and direct assistance for a growing number of abandoned children, particularly evident in Antananarivo.

Preparatory documentation for the World Bank's 1988 program also identifies a number of medium- and longer- term interventions, including a low-income housing program, promulgation of a national population policy, and a variety of health and nutrition activities. A follow-on World Bank mission is in the process of identifying for early design a variety of activities under the Social Dimensions of Adjustment Program (SDAP), an African regional program undertaken by the World Bank with funding provided by UNDP. The team will apparently recommend initiating as soon as possible a targetted feeding program and one for abandoned children as well as the provision of essential drugs, and the initiation of specific employment schemes. Looking toward the longer term, SDAP will finance a permanent household survey which will enable the Government to track the evolution of living conditions and develop a local social science capability to analyse the data collected.

Whether the World Bank decides to pursue the promulgation of a national population policy as part of its planned Health project, or independent of that effort, there is agreement among certain donors (principally UNFPA and A.I.D., as well as the World Bank) that the issue is ripe for inclusion in any agenda for policy reform. What is not yet clear is what specific policy changes are called for above and beyond the obvious need for the Government to repeal the 1920 law prohibiting the sale of contraceptives and to confront the problem posed by the growing population on development prospects. It is clear that A.I.D. will want to continue to work with private sector organizations and parastatals to strengthen the provision of family planning services. Other needed interventions will be identified in the assessment of A.I.D.'S population strategy in Madagascar now planned for mid-February 1988.

At a minimum, A.I.D. should join the World Bank and UNFPA in calling for the Government to undertake the seventeen priority studies identified during the April 1987 conference on population and development. These studies on the relationship of population growth to various economic and social sectors are considered essential underpinnings to the effort to develop a concensus on the need for and nature of a national population policy. Several of these studies have already been started, and A.I.D. will provide support for three of the most important of the seventeen through the centrally-funded OPTIONS and IMPACT projects. The studies are to be delivered, in November 1988, to the high level, inter-ministerial committee on population which has yet to be created, despite continuing, gentle donor pressure. Through the AEPRP, A.I.D. can increase the encouragement which the U.S. has been among the first to give to the establishment of this committee and the articulation of a national policy on population and development.

III. D. 3. Other Reform Issues: Conserving the Natural Resource Base

For literally hundreds of years, concern has been expressed over the depletion of Madagascar's natural resource base, as well as the threat which a growing population and traditional agriculture and forestry practices pose to its unique biological heritage. The response has been a vast number of conservation efforts, and more recently, projects intended to pioneer new cultivation practices which would lessen the adverse impact of agriculture on the resource base.

Madagascar has sought to protect its natural resources through measures which have emphasized reservation and control of protected areas, control of forest exploitation, largely top-down reforestation, rural development initiatives, and a host of essentially unenforceable rules and regulations against traditional cultivation practices. Despite these measures, over time inappropriate land use practices, coupled with a growing population, have contributed to a significant degradation in Madagascar's environment.

A.I.D. and many other donors, as well as a number of NGOs, have responded to the environmental challenge by supporting a considerable number of primarily small scale projects. A.I.D. has done so with local currency generations from the PL-480 program. A.I.D. has also added its voice to those which called for a Government-sponsored International Conference on the Conservation of Natural Resources for Development in Madagascar, held in November 1985. The objectives for the conference were to formulate a series of recommendations leading to the development of a medium- and longer- term plan for arresting natural resource degradation, and to consolidate donor support for the effort. Following the conference, the Government began work on defining a strategy for conservation and established a permanent national commission for conservation and development. Despite this history of public and private sector efforts to protect Madagascar's natural resource base and its biological diversity, however, there is as yet no concensus on what should be done. Nor has the emerging conservation strategy been translated into a prioritized action program.

A World Bank team travelled to Madagascar in October 1987 to assist the Government in planning for an environmental action plan to address a broad range of environmental issues, including conservation of the country's natural resource base, as well as protection of the quality of urban life. The Government's objectives in the development of an action plan include: (1) translating the national conservation strategy into an operational program, (2) enhancing the Government's resources (e.g. personnel, facilities, equipment) for protecting the environment, (3) reorienting investment programs to take better account of their environmental implications, (4) expanding information and education efforts, and (5) preparing reference materials on Madagascar's environment.

While A.I.D. with other donors will want to continue to support the Government in these efforts, it is not yet clear how concern over protecting Madagascar's natural resource base can be translated into a discrete element of the overall reform agenda. A.I.D. will certainly wish to encourage the development of an Action Plan for the environment which can serve as a guide for all activities in this area. The environment issue will, however, be addressed in conjunction with efforts to articulate a national policy on population and development, and as part of the on-going effort to promote improved practices in agriculture and forestry.

III. E. Conditionality/Tranching

The provision by A.I.D. of quickly disbursing balance of payments support in the form of a cash grant for imports will be conditioned on the Government's introduction of a more liberalized foreign exchange regime, presumably the OGL. Assuming that the Government puts the full OGL in place by July 1988, no further conditions precedent are planned for the provision of the cash grant, and no delay in its disbursement is anticipated.

However, by supporting achievement of the objective of a liberalized foreign exchange regime, rather than any specific form that liberalized regime might take, we can avoid tieing our hands in the event the reform process is significantly modified. Thus, if the transition to the OGL were slower than now anticipated or only partial, an unlikely alternative which should be known by the time of the PAAD design process, we would have the option of tranching the cash grant.

A.I.D. will seek to reach an understanding with the Government of Madagascar regarding a reform agenda which it will continue to pursue during the course of the program. In identifying a tentative agenda, several factors were taken into consideration. First, recognizing the lead the IMF has taken in articulating a strategy for stability and overall structural adjustment, and the World Bank's considerable progress toward identifying a reform program in the principal sectors, A.I.D. anticipates furthering these efforts rather than taking any new departures. Ideally, the opportunity will present itself to deepen or broaden elements of the on-going reform agenda. Second, every effort will be made to identify an agenda for A.I.D. which builds upon its own on-going program in Madagascar, especially in the area of liberalized food production and marketing, as well as the concern for population and preserving the natural resource base.

As discussed above, candidates for inclusion in the reform agenda - which will be explored in the course of PAAD design - include: deepening and/or broadening rice liberalization reforms, pursuing the relationship between population growth and development, preserving the natural resource base, and

budget rationalization. The first three areas are direct outgrowths of A.I.D.'s on-going efforts; the latter, which could focus on the ministries of Health, Agriculture and Public Works, is a response to the World Bank's concern that other donors join it in pursuing critically needed budget reforms, and would serve to strengthen ministries with which A.I.D. is already involved, and which are important to the success of objectives we consider of priority importance. The Section 206 reform agenda for the edible oil sector will complement the EPRP agenda for agricultural marketing price liberation.

Approaches to local currency programming, including programming generations in support of the budget (e.g. to reduce the deficit), are discussed in Section V.E.2. below. By linking local currency programming to the reforms, A.I.D. would gain leverage to pursue its reform agenda. Thus, for example, A.I.D. could utilize some or all of the local currency generations to finance a portion of the Ministry of Health's recurring costs, if the Ministry were responsive to budget rationalization initiatives. Parenthetically, this would further A.I.D.'s concern with population, inasmuch as it is this Ministry which is now beginning to promote child spacing in Madagascar.

IV. COORDINATION WITH OTHER DONORS

Madagascar's structural reform program, outlined in the preceding section, has evolved since 1983 in close association with the IMF and the World Bank. Without the government's commitment to this program, A.I.D. would not have decided to re-engage in Madagascar as it did in 1984. Since that time, A.I.D. activities have been designed and conducted in direct support of the reform program, and, consequently, in close coordination with the World Bank. Evidence of this unusually close working relationship abounds, but is most evident in the rice liberalization effort. A.I.D. provided rice through the Food for Progress Program to establish a buffer stock which was a crucial element in the liberalization agreement negotiated by the World Bank.

In such areas of the reform agenda as population and the environment, where A.I.D. has preceded the IBRD in Madagascar, this cooperation is fully reciprocated. Recognizing the important beginning which the GDRM is making with A.I.D. and UNFPA assistance in 1987 to formulate a national population policy, the World Bank has made the continuation of this process a major element in the population-health-nutrition program it is negotiating with Madagascar. And in view of the A.I.D. financed activities underway and being planned with U.S. private groups in the environment, the World Bank has invited A.I.D. to finance four of the ten members of the Bank's environmental assessment team for Madagascar, due to begin work in February 1988.

In a more general sense, the World Bank is eager for A.I.D. to continue to lend support to furthering reform in the sectors in which it is working. Specific suggestions include providing grant funding for technical assistance and short-term training, as well as urging A.I.D. to program local currency generations on-budget to further reinforce the process of budget rationalization.

V. PROGRAM ACTIVITIES

A. Overview

The Madagascar Economic Policy Reform Program (MEPRP) is proposed as a three year program with a first year funding level of $17 million. Of this amount, $15 million will be a cash grant contribution to the Open General License system, and approximately $2 million will be used to finance training, short term technical assistance, and studies linked to the policy reform agenda which will be a central feature of the program. The first year's funding will be derived in part from AEPRP funding, estimated at $10 million, and FY 1988 OYB Funding of $8 million. ($1 million of this total OYB will be used for environmental programs.) Funding levels in years two and three will be dependant on future OYB levels, but are anticipated at between $4 million and $8 million per year. A portion of these funds, $1.0 - $1.5 million per year, will be used to continue A.I.D.'s work in rice research through IRRI and environmental programs. The MEPRP will have a rolling design, in the sense that the policy reform agenda will be modified in years two and three to reflect the progress that has been made in the first year. Such modifications will be reflected in grant agreement amendments.

B. Support for a Liberalized Foreign Exchange Regime

As discussed previously, the government is publicly committed to moving during the next year from the present liberalized foreign exchange regime to a system of Open General License. Yet there is great concern among the monetary authorities over the risks that the new system poses. It is not clear that the demand for foreign exchange under the present system is an accurate predictor of demand under an OGL. The monetary authorities have voiced the fear that they may be faced with unexpectedly high demand for foreign exchange following the introduction of the OGL which would exhaust foreign exchange reserves and quickly force them into a significant devaluation. This would tend to discredit the OGL in much the same way that the initial sharp increase in rice prices at the retail level in 1985-86 tended to discredit rice market liberalization before the introduction of the buffer stock system.

The government of Madagascar ended 1986 with net foreign exchange reserves equal to SDR -145.8 million and freely available reserves equal to SDR 42.5 million. As a result of improvements in the current account over earlier projections, the 1987 balance of payments is now projected to show a surplus equal to SDR 48.7 million. This would reduce Madagascar's negative net reserve position (ignoring valuation adjustments) to SDR -97.1 million. Exactly how this will translate into freely available reserves is difficult to predict at this point, but it is likely that such reserves will stand at between SDR 45 million and SDR 90 million, or between 1.8 and 3.6 months of projected 1988 imports. (The total import bill is estimated at SDR 400 million per year). Some foreign exchange for the OGL will be provided by donors other than A.I.D., but to date the only confirmed sources are the World Bank and the IMF, and a large portion of these resources may not be available until late in the calendar year.

The Mission proposes to make the largest part of the dollar resources under this year's grant, $15 million, available to the Government of Madagascar in a single cash transfer to finance imports under the OGL. This would permit the government to more easily absorb a one-time increase in imports resulting from the introduction of the OGL. It will be made clear to the Government of Madagascar that this is the first year of a three year program, but that future year support will not be at this level. If the level of import demand should remain at a high level, the authorities should adjust the exchange rate to bring demand into line with the available supply. However, the introduction of the OGL system is likely to be accompanied by considerable uncertainty and a smoother transition will be encouraged by the availability of a fund of A.I.D. resources equal to about two weeks imports.

V. C. Policy Dialogue

A portion of the cash grant will be used to finance technical assistance, studies, and training in support of AID's reform agenda. All three types of assistance have proved to be useful venues for continuing a policy dialogue in Madagascar. It is currently estimated that as much as $2 million could be set aside for these purposes.

A variety of approaches to the provision of technical assistance will be tried. Thus, for example, it is anticipated that the Mission will want to continue some technical assistance activities now funded under the MARS project. These have included an annual visit by Elliot Berg, who has helped A.I.D. assess Madagascar's progress in both macro-economic and sectoral reforms and has conducted seminars for government officials on specific reform topics. MARS has also funded a number of special studies, such as Coopers and Lybrand's

parastatal studies under REDSO's Parastatal Divestiture IQC. Another type of technical assistance which could be provided under the program would be the services of an adviser who would provide continuing assistance in, for example, budget reform to a particular Ministry.

As A.I.D. refines its reform agenda, beginning with preparation of the AEPRP Program Assistance Approval Document(PAAD), it will be possible to be more specific about the need for certain consultancies or studies. At this juncture it is probably safe to assume that to some degree, A.I.D. grant financing will support elements of the World Bank's on-going dialogue for which IBRD loan funding is not particularly well suited or acceptable to the Government. To date, the World Bank has expressed particular interest in A.I.D. supporting technical assistance associated with budget rationalization.

V. D. Training

In his October, 1987, "Report on the Economic Reform Program in Madagascar", Elliot Berg comments, "Madagascar seems, in mid-1987, on the way to becoming one of the more dramatic cases of successful liberalization of a controlled economy." Nonetheless, he cautions that progress is "thin, uneven and fragile", largely because there seems to be "little intellectual support for the free market idea outside of the World Bank office and the U.S. Embassy." He attributes this lack of support to an absence of public education and debate "on the substance of the reforms and the nature of their intellectual foundations." If one considers that Madagascar has been accustomed to a centrally run economy from pre-colonial times to the present, the above kinds of information dissemination initiatives, as well as education/training programs, seem all the more urgently needed for reform to succeed.

Preliminary discussions with Malagasy who are involved in the reform effort indicate that they would welcome a mixture of short and long term training and education programs conducive to developing a cadre of professionals who understand, support and shape the liberalization of their country's economy within the private, public and banking sectors. According to the World Bank report "Accelerated Development in Sub-Saharian Africa", training experience has shown that for increased efficiency of resource use, formal education is needed, but, in addition, on-the-job experience is essential. Manpower-scarce, financially hard pressed developing country institutions often have difficulty assuring such training. International institutions, and bilateral ones such as A.I.D., have the means for providing such on-the-job training, and complementing it with specially designed formal training.

Short term training under the MEPRP should include study tours, on-the-job training, workshops, and any other kinds of experience which expand the capacity of reform players to perform effectively. Malagasy have suggested such initiatives as:

-non-degree training for entrepreneurs who have demonstrated ability but have lacked opportunity for classroom learning, such as three month business training offered by ISO, a French institution which collaborates with Stanford University Business School;

- on-the-job training for public employees keen on private sector experience, using AID's Private Sector Training Project; and,

- a professor from the University of Madagascar's Faculty of Law, Economics, Management and Social Sciences visiting U.S. institutions to determine which institutions offer possibilities for year-long retreading, non-degree programs for current faculty, and graduate degree programs for preparing future faculty, which could serve as the basis for designing a program of long term training .

Also appropriate would be the kind of in-country seminars that the MARS project initiated in 1986 to encourage Malagasy to understand the pros and cons of rice market liberalization. This included a workshop conducted by leaders versed in Asian and African economic liberalization experience. The second workshop funded under MARS in 1988 will include leadership by Malagasy who, after completing a study tour of Asian countries with economic liberalization in action, will be prepared to share observations with their compatriots.

Long term training will assure the retreading of both public and private sector Malagasy who hold higher degrees, but need extra study to understand and support the economic reforms now underway. Malagasy have suggested as a model the year long course at M.I.T.'s Sloan School of Business. Similar programs likely are available in French-speaking Canadian universities, such as the University of Montreal.

Ph.D programs would target Malagasy with demonstrated potential for teaching in higher education institutions charged with preparing graduates to plan and implement economic reform. Areas of specialization could include such subjects as trade and exchange rate policy, economic decision-making, the proper role of government, and organization and management.

V. E. Local Currency Programming - Criteria

The cash grant will generate an equivalent amount of local currencies which will be placed in a special account at

the Central Bank. These local currencies will be available for programming with A.I.D. approval. However, the principles for programming these generations will differ radically from the way in which such funds are now handled.

With A.I.D. approval, the Government is currently involved in programming considerable amounts of local currencies generated by PL 480 Title I programs and the CIP component of MARS, as well as smaller amounts generated by monetized portions of PL 480 Title II emergency programs and the FY 1986 sugar quota offsets. With the exception of counterpart which has been set aside in a trust fund to finance the local currency costs of A.I.D.'s Madagascar operations, generations finance projects in the GDRM's Public Investment Program, particularly in agriculture, where the priority is given to the rehabilitation of productive and transport infrastructure. The FY 1987 PL480 Title I Agreement also permits the use of generations to support UNICEF's national immunization/child survival program and the national population census. Other criteria applied in project selection include: (1) priority given to large scale projects financed in foreign currency by A.I.D. and other donors, (2) use of local currencies to supplement and not supplant other sources of funding, and (3) activities financed should lead to self-sustaining efforts.

At the present time, approximately 200 local currency-financed activities are underway, while another 160 or so have been completed in the past three years. A combination of direct hire and local PSC staff monitor the program. In the face of recent Agency guidelines which require A.I.D. to attend more carefully to both the design and implementation of local currency-financed activities, the Mission can no longer assume the management burden of overseeing so large a project portfolio.

Furthermore, the World Bank has expressed concern that those donors which continue to projectize local currency generations, namely the United states, the French and the European Development Fund, are undermining efforts at budget rationalization. Therefore, the Bank recommends that by programming future local currency generations for recurring costs of the Government's budget, we will both assist it to meet its budget deficit and gain leverage for pursuing budget rationalization as part of our reform agenda.

For these reasons, local currencies, other than those required to replenish the trust fund, will be programmed in their entirety in support of the Government's budget reform activity, as described below. In the event the Mission identifies future priority uses for local currency, it will have ample other resources to draw from, including existing local currencies which are as yet unprogrammed and the sizeable generations which will result from the new Section 206 food assistance activity planned to begin in FY 1988.

As discussed in Section III.C., the Government is currently undertaking a budgeting reform process which is designed to increase the allocative and economic efficiency of government expenditures. Local currencies generated by the MEPRP can be well utilized to support these reform activities through the attribution of local currency generations to the recurrent budget. Specifically, the use of MEPRP counterpart in the agriculture, public works, and health budgets would, in the first instance, bring a major quantity of donor counterpart which is currently an off-budget resource onto the budget for planning and expenditure purposes. Furthermore, in addition to supporting the budget rationalization, attribution of our counterpart to these sectors has the added benefit of funding salaries and other recurrent costs related to those sectors which are important to the success of A.I.D. funded projects.

Resources provided for the Ministry of Agriculture's budget, for example, could be utilized for salary and recurrent costs associated with, inter alia, the extension of results of rice research activities. The Health Ministry offers a slightly different example; support for the recurrent budget in health will again provide resources for salaries and other recurrent costs which in turn will assist in the provision of urban and rural health services, and in the delivery of information regarding child spacing and family planning activities. Finally, attribution to the budget of the Public Works Ministry, especially for transport infrastructure and water delivery program support, would address concerns that we and the Government have regarding the transport of people and commodities within the country, and the maintenance of transport, irrigation, and water delivery systems. Before the PAAD is completed, consideration should be given to the manner in which these services can be expanded to help support the government's interest in maternal/child health and the amelioration of hardships caused by the structural adjustment program.

In addition to providing support for moving revenues and expenditures on-budget and funding ongoing budget activities, attribution of the local currency generations to the recurrent budget has several other advantages. First, as the transfer of a real, on-budget resource, it will help reduce the Government's budget deficit. Furthermore, while the funds are generated by a transfer of resources from the private to the public sector, the reduction in the budget deficit will have the impact of increasing resources available to the private sector to the extent that domestic borrowing to finance recurrent deficits is reduced.

V. F. Grant Tracking Requirements

A.I.D.'s recently issued "ESF Cash Transfer Assistance--Amplified Policy Guidance" addresses the implementation of statutory requirements that separate accounts for both dollars and local currency be established pursuant to cash transfer agreements. Although these tracking requirements formally pertain only to ESF cash grants at this time, they will be applied to the MEPRP program as well, inasmuch as it is the intent of Congress that A.I.D. improve its ability to account for both dollars provided in the form of cash grants and resulting local currency generations.

Specifically, the guidance requires that all countries receiving cash transfer assistance in excess of $5 million establish a separate account into which will be placed the dollar assistance, as well as a separate account for deposits of local currencies generated by the grant. Thus, the Government will be expected to account for the disposition of dollars after disbursement by A.I.D.. Toward this end, the dollar account into which the grant is deposited and from which funds are released for agreed-upon uses may not be co-mingled with other funds. Prior to any release, A.I.D. and the Government will agree on the general uses of the dollars, in this case to finance imports under the OGL, which will be reflected in the cash transfer assistance agreement.

Appropriate procedures for specifying and tracking uses of both dollars and local currencies released from the special accounts will be worked out at the time of the PAAD design. Madagascar's foreign exchange and import regime, the integrity of its accounting system, and other factors will be taken into account. Mechanisms by which A.I.D. will monitor both the uses of the cash grant and local currency generations will also be worked out in the course of PAAD design. A related issue to be addressed at that time will be the extent and frequency of reporting requirements on both special accounts.

Finally, the agreement will include appropriate audit and redeposit provisions.

V. G. Management/Staffing Implications

Plans to augment the direct hire staff of the Mission should include the addition of a program economist to monitor progress in Madagascar's reform process. This will involve maintaining close contact with the Government and working closely with the resident World Bank staff, as well as with visiting IMF and World Bank missions and with other donors, especially the French, who are supporting the reform agenda.

The project development officer, who is already on-staff, will share responsibility for implementing both the cash grant and local currency aspects of the program.

It may prove impossible to recruit a well qualified USDH program economist before the end of FY 1988. In this event, the Mission may wish to consider securing the services of a PSC to assist the AID Rep and PDO in negotiating the agreement with the Government, and initiating implementation.

Once the PAAD design is further along, the Mission may also want to consider bringing in one or more short term PSCs to assist it in pursuing its reform agenda with the Government. Assuming the Mission will proceed with plans to secure the services of a natural resources/agricultural expert in conjunction with its on-going program, obvious candidates for additional short-term PSC slots include specialists in budget rationalization and population.

In addition, REDSO/ESA will continue to provide support for the program during both the design and implementation stages.

VI. PAAD DEVELOPMENT AND AUTHORIZATION

A. Next Steps

1. Consultative Group and IMF/IBRD Reviews

Preparations are now underway for the next Consultative Group meeting for Madagascar, scheduled to be held in Paris the last week of January 1988. At this meeting, the GDRM will present its economic program for the coming year and solicit donor support for its public investment program. This meeting will be followed immediately by an appraisal mission for the World Bank's next Structural Adjustment Loan, which is scheduled for submission to the IBRD Board in June of 1988. An IMF team is also scheduled to come in Madagascar in early February to begin negotiation on a Standby Agreement which will replace the current Standby due to expire in March of 1988.

These World Bank and IMF negotiations should result in the establishment of a clear policy reform agenda for Madagascar, which will serve as the foundation for the development of the A.I.D. Economic Policy Reform Program PAAD and the Section 206 program.

2. Studies/Consultancies

Much of the additional study needed of key economic issues - liberalization of the import regime, budget

rationalization, public expenditure control, financial sector reform, and export marketing reform - will be undertaken by the IBRD and IMF missions in February. The PAAD Design team will review the reports prepared by the IBRD and IMF teams and determine if adequate information has been provided for the elaboration of the AID reform agenda.

Another area where further study is needed is that of the status of environmental policy, and possible interventions for USAID to encourage the GDRM in establishing an action program for the environment. During the month of October 1987, the World Bank requested A.I.D. participation in a comprehensive environmental assessment for Madagascar, planned as the World Bank's first such assessment anywhere in the world. Funding for the four members of the team who would be designated by A.I.D. has been requested from the Natural Resources Management Support Project. If the financing can be put in place, this assessment would be carried out in February/March 1988, a timing which would permit substantive input into the design of the EPRP/PAAD.

Population policy is a final area where additional study is needed to assess the appropriateness of including reform in this sector in the reform agenda of the EPRP. If the required funding and the technical expertise can be obtained, an assessment of USAID/Madagascar's population strategy will be carried out in February 1988 with a view toward identifying the next steps that should be taken to support the development of a national population policy for Madagascar.

3. Initial Environmental Examination

There are no anticipated negative impacts on the environment from the proposed cash grant, training, and consultancies, and the PAIP design team recommends that a categorical exclusion be approved for the Madagascar Economic Policy Reform Program. The draft initial IEE can be found in Annex B.

V. B. Design and Authorization Schedule

The PAAD design team will consist of the following members:

Project Development Officer and Team Leader	REDSO/ESA
Economist	REDSO/ESA
Regional Legal Advisor	REDSO/ESA
Agricultural Economist	Contract
Training Officer	PSC

Although not included within Madagascar's original request for

FY 1988 PD&S funds, it is now anticipated that approximately $17,000 will be needed to fund the services of an agricultural economist for the design effort.

The following is the proposed schedule for design and authorization of the MEPRP:

Date	Action
December 17, 1987	REDSO/ESA PAIP Review
January 1988	A.I.D./W PAIP Review
January-February 1988	Preparatory Studies Undertaken
March 1988	PAAD Design
Late April	A.I.D./W PAAD Review
May 1988	PAAD Authorization
May 1988	Grant Agreement Prepared
June 1988	Grant Agreement Signed

V. C. Other Design Issues

An issue which arose during the EPRP PAIP design which requires AID/W consideration is the FAA requirement for a 25 % host country contribution to DA funded programs. Under the current guidelines, Madagascar is not eligible for a waiver of this requirement because it is not on the U.N. list of relatively least developed countries. The proposed EPRP program would consist primarily of a cash grant for imports under an open general licensing (OGL) system, together with some funding for training, studies and short term technical assistance related to the reform program. The PAIP design team does not believe that the Government of Madagascar should be required to make a separate 25% contribution to what is essentially a cash grant, particularly since the GDRM will be contributing the majority of the foreign exchange needed to support the OGL system. A special "waiver" of the FAA requirement for a host country contribution should therefore be considered.

VI. D. Program Risks

The liberalized foreign exchange and import regimes which Madagascar is putting in place, as well as the emerging sectoral reform agendas which have been identified for support by the World Bank, A.I.D., and other donors could provoke opposition within the Government or in the general population which would jeopardize further design, negotiation and implementation of the EPRP. Indeed, unexpected wrinkles should be anticipated, as policy reform is associated with risk and uncertainty surrounding the actual outcomes and unforeseen negative consequences.

The PAIP design team was sensitive to a number of contradictory

developments. On the one hand, an IMF team, here in November to review the status of the current standby, judged the Government to be out of compliance and secured agreement to accelerate the pace of certain key structural reforms as the price for not suspending the Arrangement before the upcoming Consultative Group meetings. A concurrent World Bank team, on the other hand, left behind an Aide Memoire expressing concern over the social dimensions of the adjustment process and calling for both near- and longer-term actions to ameliorate the lingering consequences of poverty. Thus, pressure is building on the part of certain donors, for an immediate targetted feeding program and for assistance to abandoned children, and in the medium term, for attention to housing, population, and health and nutrition. A follow-up Bank team began identifying specific activities to be undertaken under the Bank's Social Dimensions of Adjustment Program, a regional facility of the World Bank, the African Development Bank, and the UNDP.

Others, including Elliot Berg, have expressed concern over what they see as the fragility of the Malagasy commitment to the reform process, as well as that of certain key donors. This manifests itself in frequently expressed skepticism both about whether the reforms will have their intended consequences and about whether certain key figures are, in any case, supporting the reform effort.

Malagasy economic reform prospects are improved by the apparent continued acceptance of the process at the top-leadership level, as evidenced by commitment made to the IMF during its most recent visit. However, despite widespread dissatisfaction with the economic situation which prevailed in the early 1980s, there is not yet much evidence of generalized optimism that the reform process will improve conditions substantially. Nor is there yet any evidence of popular support for the program, with the notable exception of the rice buffer stock program. Therefore, as presidential elections approach, a key question is whether the Malagasy will stay the course of reform over the medium-to-longer term.

The timing of A.I.D.'s EPRP design process is fortuitous. The PAIP team arrived on the heels of both an IMF assessment team and a number of important World Bank missions. While the IMF successfully renegotiated the terms of the current Standby, Bank staff paved the way for a number of new reform initiatives in areas of interest to A.I.D., including the environment and population and health. Both institutions will field follow-up missions in early February, including an IMF team to negotiate the next Standby. Thus, A.I.D. will know a great deal more about both Malagasy and donor commitment to the reform process before it fields its own PAAD design team, thus minimizing the risk of designing an unviable program.

Furthermore, to reduce the risk that implementation of the reform program, particularly of the OGL, will be only partial or slower than anticipated, the PAIP provides for the possibility of tranching the cash grant. Similarly, by attaching some conditionality to A.I.D.'s offer to make local currency generations available to reduce Madagascar's budget deficit, A.I.D. will have opportunities to continue to assess the extent of Malagasy commitment. For this reason, although significant risks remain, the PAIP team believes that they are sufficiently manageable to warrant the development of the PAAD.

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Table 1

Origin and Uses of Gross Domestic Product
(Billion 1984 Malagasy Francs)

	1981	1982	1983	1984	1985	1986
Agriculture	528.5	549.7	562.7	580.6	591.7	605.0
Mining & Manufact.	235.1	201.5	203.3	213.9	223.5	219.6
Pub. Sect. Services	142.7	144.1	145.4	128.0	129.2	130.0
Other Services & Other	452.4	438.9	434.8	446.6	455.8	456.1
GDP at Market Prices	1358.7	1334.2	1346.2	1369.1	1400.2	1410.7
Net Import of Goods & NFS	108.5	113.9	85.7	59.7	49.2	59.6
Consumption	1248.7	1269.9	1255.0	1243.0	1260.1	1272.3
Private	1042.4	1070.3	1054.1	1058.0	1070.5	1081.9
Public	206.3	199.6	200.9	185.0	189.6	190.4
Gross Investment	218.4	178.2	176.8	185.7	189.3	198.0
GDP at Market Prices	1358.6	1334.2	1346.1	1369.0	1400.2	1410.7

(Percent of total)

	1981 %	1982 %	1983 %	1984 %	1985 %	1986 %
Agriculture	38.9	41.2	41.8	42.4	42.3	42.9
Mining & Manufact.	17.3	15.1	15.1	15.6	16.0	15.6
Pub. Sect. Services	10.5	10.8	10.8	9.3	9.2	9.2
Other Services & Other	33.3	32.9	32.3	32.6	32.6	32.3
GDP at Market Prices	100.0	100.0	100.0	100.0	100.0	100.0
Net Imports of Goods & NFS	8.0	8.5	6.4	4.4	3.5	4.2
Consumption	91.9	95.2	93.2	90.8	90.0	90.2
Private	76.7	80.2	78.3	77.3	76.5	76.7
Public	15.2	15.0	14.9	13.5	13.5	13.5
Gross Investment	16.1	13.4	13.1	13.6	13.5	14.0
GDP at Market Prices	100.0	100.0	100.0	100.0	100.0	100.0

(percent change)

	1982 %	1983 %	1984 %	1985 %	1986 %
Agriculture	4.0	2.4	3.2	1.9	2.2
Mining & Manufact.	-14.3	0.9	5.2	4.5	-1.7
Pub. Sect. Services	1.0	0.9	-12.0	0.9	0.6
Other Services & Other	-3.0	-0.9	2.7	2.1	0.1
GDP at Market Prices	-1.8	0.9	1.7	2.3	0.7
Net Import of Goods & NFS	5.0	-24.8	-30.3	-17.6	21.1
Consumption	1.7	-1.2	-1.0	1.4	1.0
Private	2.7	-1.5	0.4	1.2	1.1
Public	-3.2	0.7	-7.9	2.5	0.4
Gross Investment	-18.4	-0.8	5.0	1.9	4.6
GDP at Market Prices	-1.8	0.9	1.7	2.3	0.7

Source: IMF, RED, FEB. 13, 1987 Table 1 and mission estimates

Table 2

Production of Major Cash Crops, 1981-86 (1)
(in thousands of tons)

		1981	1982	1983	1984	1985	1986 (Prelim.)
Export crops							
Coffee (2)	Production	83.5	81.2	80.8	81.4	78.5	78.5
	Marketed	58.5	52.7	47.1	65.2	46.6	50.0
Vanilla	Production (3)	4.3	5.5	2.2	6.9	7.0	3.3
	Marketed (4)	1.0	1.2	0.5	1.5	1.6	0.7
Cloves	Production	10.8	9.9	4.2	18.0	13.5	7.1
	Marketed	10.2	15.0	2.3	16.0	8.0	6.0
Pepper	Production	2.9	2.6	2.6	2.6	2.8	2.8
	Marketed	1.9	2.2	2.0	2.2	2.1	2.3
Cocoa	Production	1.8	1.9	2.8	3.0	2.3	2.4
	Marketed	1.7	1.8	2.7	2.9	2.2	2.3
Butter beans	Production	5.0	6.2	5.8	7.1	5.8	6.0
	Marketed	3.0	...	3.9	6.0	5.0	5.0
Sisal	Production (5)	15.4	15.1	12.5	19.8	19.8	19.8
Industrial Crops							
Cotton (6)	Production (5)	28.0	25.9	26.3	32.5	42.9	43.0
Sugar (7)	Production	1420.4	1408.6	1615.8	1660.0	1744.0	1950.0
	Marketed	1055.0	848.0	958.8	1069.7	1138.2	1380.0
Groundnuts	Production	32.9	29.6	32.3	31.5	31.5	32.0
	Marketed	20.0	20.1	23.3	18.6	18.6	18.5

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

(1) Data on total production are approximate; data on marketed production are more accurate.
(2) Unroasted coffee.
(3) Green vanilla.
(4) Prepared vanilla (4.6 kg green = 1 kg prepared).
(5) Most of the production is marketed.
(6) Seed cotton.
(7) Sugarcane.

Table 3

Madagascar: Nominal and Real Paddy Producer Prices, 1961-86

	Producer price paddy (FMG/kg)	Producer Prices (1) Nominal (1975=100)	Producer Prices (1) Real (1975=100)	Estimated Effective Producer Price (2) FMG/kg	Estimated Effective Producer Price (2) Nominal (1975=100)	Estimated Effective Producer Price (2) Real (1975=100)
1961	8.0	27	54			
1962	9.0	30	59			
1963	9.0	30	58			
1964	11.0	37	67			
1965	11.0	37	64			
1966	12.6	42	71			
1967	13.0	43	73			
1968	13.4	45	74			
1969	13.6	45	73			
1970	14.2	47	74			
1971	15.0	50	74			
1972	15.0	50	74			
1973	15.0	50	66			
1974	25.0	83	90			
1975	30.0	100	100			
1976	35.0	117	111			
1977	35.0	117	108			
1978	35.0	117	101			
1979	38.0	127	96			
1980	43.0	143	92			
1981	47.0	157	77			
1982	60.0	200	75			
1983	65.0	217	68	81	271	85
1984	75.0	250	71	90	300	86
1985	83.0	277	71	103	343	89
1986	100.0	334	73	215	716	159

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

(1) Until 1983 the minimum producer price was the effective producer price. With the liberalization measures introduced in May 1983 the actual prices paid to producers exceeded the minimum producer price.
(2) Prices reportedly paid to producers in areas adjacent to Antananarivo.

Table 4

Production and Export of Major Minerals, 1981-86

	1981	1982	1983	1984	1985	1986 Prov.
Production (thousand tons)						
Chromite	99.7	44.2	42.9	59.8	126.7	100.0
Graphite	16.0	15.2	13.5	14.1	14.7	15.0
Exports (thousand tons)						
Chromite	80.8	63.7	59.4	92.4	103.2	104.0
Graphite	16.3	14.9	11.7	14.5	16.1	16.0
Export value (millions of SDRs)						
Chromite	4.8	3.6	2.7	4.1	4.7	5.0
Graphite	7.7	7.1	5.5	6.0	7.2	7.9
Unit value (SDR per ton)						
Chromite	60	56	45	44	46	48
Graphite	470	477	470	417	447	491

Sources: Data provided by the Malagasy authorities (National Institute of Statistics and Economic Research; and Customs Office); and staff estimates.

Table 5

Index of Manufacturing and Mining Production, 1981-86

(1981 = 100)

	Weight (1) (in percent)	1981	1982	1983	1984	1985	1986 Prov.
Food processing	9.0	100	79	82	64	77	93
Beverages	2.9	100	96	132	118	129	141
Tobacco	2.6	100	110	94	111	123	114
Textiles	25.3	100	93	92	85	80	87
Shoes	4.0	100	88	76	56	57	61
Chemicals	5.9	100	72	86	79	96	101
Petroleum products	40.8	100	94	50	16	82	20
Construction materials	1.4	100	104	107	135	101	121
Extractive Industries	3.5	100	85	76	76	110	107
Paper	4.3	100	91	93	90	96	109
Electrical Applicances	0.2	100	158	1024	1091	1004	1204
Total	100.0	100	91	76	57	87	67
(without petroleum products)		(100)	(89)	(93)	(86)	(90)	(99)

Sources: Data provided by MIEM; and staff estimates.

(1) Based on 1981 prices.

Table 6

Pattern of Household Consumption in CPI

(in percent)

	Domestic unprocessed (1)	Processed, domestic content only (2)	Processed, domestic, & imported content (3)	Imported, finished products (4)	Total
Traditional households					
Food	47.35	10.79	1.67	0.54	60.35
Rice	(15.98)	(--)	(--)	(--)	(15.98)
Fruits and vegetables	(6.21)	(--)	(--)	(--)	(6.21)
Other	(25.16)	(10.79	(1.67)	(0.54)	(38.16)
Fuel and electricity	1.99	5.97	1.18	--	9.14
Domestic services	--	1.82	--	--	1.82
Maintenance, clothing, and medicine	--	9.06	3.66	2.13	14.85
Miscellaneous	--	10.16	2.71	0.97	13.84
Total	49.34	37.80	9.22	3.64	100.00
Modern households					
Food	12.67	21.93	5.57	4.99	45.16
Fruit and vegetables	4.43	--	--	--	4.43
Other	8.24	21.93	5.57	4.99	40.73
Fuel and electricity	0.11	3.79	2.18	--	6.08
Domestic services	--	11.26	--	--	11.26
Maintenance, clothing and medicine	--	8.08	2.21	7.70	17.99
Miscellaneous	0.56	6.58	7.59	4.78	19.51
Total	13.34	51.64	17.55	17.47	100.00

Source: Data provided by the Malagasy authorities.

(1) Domestic, unprocessed - All domestically produced goods and services which do not require extensive processing.
(2) Processed domestic content only - All locally manufactured products for which all raw materials are domestically produced.
(3) Processed, domestic and imported contents - All locally manufactured products for which raw materials are wholly or partly imported.
(4) Imported finished products - All goods which are imported in the form in which they are consumed, i.e., no local value added.

Table 7

Central Government Budgetary Position

(percent of GDP)

	1983 %	1984 %	1985 %	1986 %
Total budgetary rev.	11.5	12.3	12.6	11.7
Tax revenue	11.1	11.7	12.2	11.4
Taxes on inc. & prof.	2.2	2.7	2.1	2.2
Companies	1.0	1.3	1.0	0.8
Individual	1.0	1.2	1.0	1.2
Capital income	0.1	0.2	0.2	0.1
Other	.0	0.1	.0	.0
Taxes on property	0.1	0.1	0.1	0.1
Taxes-goods & serv.	4.1	3.9	3.6	3.6
Value added	1.9	1.8	1.7	1.6
Excises	1.2	1.2	1.1	1.1
Fisc. Monop. Prof	0.9	0.9	0.8	0.8
Other	0.1	0.1	0.1	0.1
Taxes on foreign trade	4.6	4.8	6.2	5.4
Import duties	3.5	3.7	4.4	3.8
Export duties	1.1	1.1	1.8	1.6
Other taxes	0.1	0.1	0.2	0.2
Non-tax revenue	0.4	0.6	0.3	0.3

Central Government Expenditure

	1983 %	1984 %	1985 %	1986 %
Total current exp.	11.9	12.6	12.6	11.5
Personnel exp.	7.2	7.2	7.0	6.5
Goods & Services	2.1	2.1	2.6	1.8
Interest-Gov't debt	1.2	1.9	1.8	1.8
External	1.0	1.6	1.4	1.4
Internal	0.3	0.3	0.3	0.4
Transfers	1.4	1.5	1.3	1.4
Total budgetary capital expenditures	4.0	4.1	4.2	3.8
Memo: non-budgetary capital expenditures	3.1	4.0	3.2	3.1

Table 8

Government Personnel Expenditure
and Number of Civil Servants, 1981-86

	1981	1982	1983	1984	1985	1986 Proj.
Personnel expenditure						
Outlays in billions of Malagasy francs (1)	73.0	85.8	88.1	98.6	109.0	118.0
Of which: wages and salaries	(68.0)	(80.7)	(81.9)	(92.0)	(101.7)	(109.0)
Annual change in percent	14.1	17.5	2.6	11.9	10.6	8.3
As percent of current budgetary expenditure	65.1	67.3	61.6	57.1	55.5	56.6
As percent of total budgetary expenditure (2)	48.9	55.4	51.1	49.6	47.4	48.0
As percent of total government expenditure	30.7	35.9	33.0	31.8	33.6	33.5
As percent of GDP	9.2	8.6	7.2	7.0	7.2	6.4
Civil servants						
Total number at end-December	121,156	126,023	127,500	128,500	129,000	129,50
Annual change in percent	2.6	4.0	1.2	0.8	0.4	0.4

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

(1) Excluding medical expenses.
(2) Consisting of current budgetary expenditure and locally financed capital outlays.

Table 9

Revenue and Expenditure of the Export Stabilization Fund (FNUP), 1981-86

(in billions of Malagasy francs)

		1981	1982	1983	1984	1985	Projection 1986
I.	Revenue	15.2	26.4	36.3	61.8	49.3	54.0
II.	Expenditure	18.0	6.1	13.0	16.6	14.2	15.2
	Current expenditure	11.0	4.2	10.5	12.6	13.1	12.2
	Operating expenditure(1)	(2.6)	(2.8)	(9.5)	(10.9)	(12.2)	(12.2)
	Price stabilization	(8.4)	(1.4)	(1.0)	(1.7)	(0.9)	(0.0)
	Capital expenditure (2)	7.0	1.9	2.5	4.0	1.1	3.0
III.	Surplus or deficit (-) (= I - II) (3)	-2.8	20.3	23.3	45.2	35.1	38.8

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

(1) Including transportation, storage, and marketing expenses, and overhead.
(2) Mostly construction of rural roads.
(3) Deficit was financed by the Treasury, and surpluses were used for financing other government operations, as consolidated in Table 6.

Table 10

Summary Accounts of the Central Bank, 1981-86

(in billions of Malagasy francs; end of period)

	1981	1982	1983	1984	1985	1986 Sept.
Net foreign assets	-47.9	-118.2	-130.8	-193.5	-137.9	-140.4
Foreign assets	6.6	9.4	17.3	44.8	31.3	76.0
Foreign liabilities	54.5	127.6	148.1	238.3	169.2	216.4
IMF	(21.8)	(39.2)	(43.4)	(54.7)	(52.3)	(57.9)
Arrears	(34.0)	(46.3)	(77.0)	(152.3)	(91.6)	(104.2)
Other liabilities	(-1.3)	(42.1)	(27.7)	(31.3)	(25.3)	(54.3)
Total claims	233.9	275.3	340.8	389.9	408.0	412.1
Claims on Government (net)	223.8	257.0	305.7	345.1	370.7	382.3
Credit to Government	267.1	339.8	422.0	514.7	599.3	663.6
Ordinary advances	(220.9)	(291.0)	(381.7)	(476.7)	(558.9)	(622.7)
Rice marketing financing	(40.0)	(42.4)	(35.7)	(34.5)	(36.0)	(36.2)
On-lending	(2.5)	(2.7)	(2.7)	(1.7)	(1.0)	(0.8)
Other	(3.7)	93.7)	(1.9)	(1.8)	(3.5)	(4.0)
Government deposits	43.3	82.8	116.3	169.6	228.6	281.3
Claims on state enterprises	8.6	18.3	26.9	35.9	32.4	29.8
Claims on banks	1.5	--	8.2	8.9	4.8	--
Assets = liabilities, net	186.0	157.1	210.0	196.4	270.1	271.7
Reserve money	103.6	99.9	96.5	104.7	108.5	162.2
Currency outside banks	83.1	90.4	75.7	89.9	96.2	114.5
Currency in banks	1.7	2.1	2.0	2.5	2.1	2.7
Bank deposits	18.8	7.4	18.8	12.3	10.2	45.0
Long-term foreign liabilities	94.1	140.8	269.2	376.3	520.0	685.5
of which: rescheduling agreements	(49.9)	(87.5)	(193.1)	(301.4)	(471.4)	(654.8)
Other liabilities (net)	-11.7	-83.6	-155.7	-284.6	-358.5	-576.0
of which: valuation adjustments	(--)	(-55.1)	(-108.6)	(-200.7)	(-220.1)	(-390.4)

Source: Data provided by the Malagasy authorities.

Table 11

Summary Accounts of the National Banks, 1981-86

(in billions of Malagasy Francs; end of period)

	1981	1982	1983	1984	1985	1986 Sept.
Reserves	20.5	12.0	20.8	14.8	12.3	47.7
Cash	1.7	2.1	2.0	2.4	2.1	2.7
Deposits with Central Bank	18.8	9.9	18.8	12.3	10.2	45.0
Net foreign assets	-1.9	7.3	9.4	19.1	20.2	19.3
Foreign assets	13.2	16.6	17.7	29.3	29.8	31.9
Foreign liabilities	15.1	9.3	8.3	10.3	9.6	12.6
Claims on Government (net)	-0.5	-3.3	-15.9	-23.4	-28.1	-28.8
Credit to Government	17.0	16.8	9.0	9.4	9.8	10.4
Government deposits	17.5	20.1	24.9	32.8	37.9	39.2
Claims on private sector and state enterprises	166.2	201.8	232.9	295.4	355.3	414.2
Assets = liabilities (net)	184.3	217.8	247.2	305.9	359.7	452.4
Deposits	142.9	161.5	171.5	206.7	238.5	307.5
Demand deposits	110.4	117.3	121.2	149.7	142.3	167.3
Time deposits	32.5	44.2	50.3	57.0	96.2	140.2
Borrowing from Central Bank	1.5	--	8.2	8.9	4.8	--
Other liabilities (net)	39.9	56.3	67.5	90.3	116.4	144.9
Of which:						
Long-term domestic borrowing	(4.9)	(4.5)	(4.8)	(5.3)	(7.6)	(8.0)
Long-term foreign borrowing	(14.7)	(16.0)	(15.0)	(11.7)	(8.1)	(5.7)
Related data						
Customs duty bills (1)	3.9	4.5	2.7	2.7	4.6	4.4
Subtotal	13.6	13.7	13.9	14.0	14.1	11.9
Post office checking deposits	(3.9)	(4.0)	(4.3)	(4.3)	(...)	(4.6)
Private sector demand deposits with the Treasury	(9.7)	(9.7)	(9.7)	(9.7)	(...)	(7.3)
Private sector savings deposited with the National Saving Fund	5.3	5.5	5.5	5.2	4.6	5.3

Source: Data provided by the Malagasy authorities.

(1) Credit to the private sector from the Treasury in the form of customs receipts to be collected.

Table 12

Interest Rates Applied by the National Banks, 1985-86

(In percent per annum)

	1985	1986 (1)
Deposits		
Sight deposits	0.66- 4.45	0.79- 4.46
Time deposits		
Less than 6 months	4.00- 8.75	4.00- 9.00
6 to 12 months	8.00-12.00	8.00-12.00
1 to 2 years	13.50-14.00	13.50-14.00
2 to 3 years	13.50-16.00	13.50-16.00
Over 3 years	16.00-18.00	16.00-18.00
Certificates of deposit		
Less than 6 months	7.50	7.50
6 to 12 months	7.50- 8.50	7.50-10.50
1 to 2 years	8.50-11.00	8.50-11.00
2 to 3 years	9.50-11.50	9.50-11.50
3 to 4 years	10.50-12.50	10.50-12.50
4 to 5 years	12.50-13.00	12.50
Over 5 years	12.50-13.50	12.50
Loans		
Short-term loans		
F1	14.00-16.50	14.00-16.00
F2	13.00-18.00	12.00-17.50
F3	15.00-21.00	15.00-19.00
F4	16.00-21.00	15.00-19.00
F5	13.00-16.50	12.75-15.00
F6	15.00-22.00	15.00-22.00
F7	16.50-19.00	16.50-19.00
Medium-term rediscountable loans	14.00-19.00	13.00-20.00
Medium-term non rediscountable loans	18.00-20.00	18.00-20.00
Long-term loans	11.00-19.00	11.00-19.00

Source: Data provided by the Malagasy authorities.

(1) First six months.

Table 13

Exports, f.o.b. 1981-86
(Value in millions of SDRs, volume in thousand tons, and unit value in SDR per kg unless otherwise specified)

	1981	1982	1983	1984	1985	1986 (prel.)
Coffee						
Value	94.74	84.90	105.97	137.64	101.48	123.10
Volume	56.90	53.90	50.50	53.80	44.70	51.00
Unit price	1.66	1.60	2.10	2.56	2.27	2.40
Cloves						
Value	55.31	60.80	15.46	35.69	34.70	29.96
Volume	7.70	9.40	2.00	6.30	11.50	11.14
Unit price	7.17	6.40	7.84	5.69	3.01	2.69
Vanilla						
Value	23.39	42.40	58.37	51.33	43.00	39.95
Volume	0.60	0.90	1.10	0.80	0.60	0.80
Unit price	36.83	47.80	53.11	62.07	68.47	49.95
Pepper						
Value	2.85	2.50	3.09	3.90	5.14	4.48
Volume	2.00	2.20	3.20	2.80	2.62	2.00
Unit price	1.40	1.20	0.96	1.39	1.96	2.24
Shellfish						
Value	14.25	19.10	22.22	21.31	21.75	28.81
Volume	3.30	4.00	3.60	3.80	4.26	5.20
Unit price	4.37	4.80	6.19	5.61	5.11	5.54
Sugar						
Value	7.60	3.10	11.39	5.48	9.35	5.57
Volume	12.20	10.70	32.30	17.40	32.80	10.50
Unit price	0.62	0.20	0.35	0.31	0.29	0.53
Meat						
Value	3.92	2.40	1.59	4.12	1.58	0.01
Volume	2.20	1.10	0.80	3.50	1.27	0.05
Unit price	1.81	2.20	2.03	1.18	1.24	0.22
Cocoa						
Value	2.16	2.10	3.05	4.42	2.90	3.12
Volume	1.80	1.40	2.30	2.50	1.60	2.10
Unit price	1.20	1.50	1.32	1.77	1.79	1.49
Cotton cloth						
Value	13.25	15.20	10.14	11.00	12.22	8.30
Volume	7.50	8.00	4.50	4.40	4.70	3.07
Unit price	1.76	1.90	2.24	2.47	2.61	2.70
Sisal						
Value	5.32	5.70	3.74	4.39	2.76	3.00
Volume	13.40	15.40	10.60	12.00	7.44	10.60
Unit price	0.40	0.40	0.35	0.36	0.37	0.28
Petroleum products						
Value	12.71	9.80	9.25	--	4.66	3.17
Volume	143.12	65.40	57.10	--	32.95	27.96
Unit price	0.09	0.20	0.16	--	0.14	0.11
Chromite						
Value	4.78	3.60	2.66	4.07	4.74	5.04
Volume	80.80	63.70	59.40	92.40	103.18	104.00
Unit price	0.06	0.06	0.04	0.04	0.05	0.05
Graphite						
Value	7.66	7.10	5.50	6.04	7.19	7.85
Volume	16.30	14.90	11.70	14.50	16.13	16.00
Unit price	0.47	0.50	0.47	0.42	0.45	0.49
Essence of cloves						
Value	2.40	2.40	2.68	6.26	3.63	2.60
Volume	0.70	0.70	0.80	1.80	1.14	0.80
Unit price	3.46	3.70	3.39	3.51	3.23	3.24
Other items						
Value	17.30	19.90	19.79	23.93	19.46	21.16
Re-exports						
Value	14.00	15.40	14.80	5.60	--	--
Total	281.64	296.40	289.70	325.18	274.48	286.20

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

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Table 14

Composition of Imports, c.i.f., 1981-86

(In millions of SDRs)

	1981		1982		1983		1984		1985		1986	
	Value	Percent	Value	Percent	Value	Percent	Value	Percent	Value	Percent	Value	Percent
Equipment goods	161.6	31.3	105.8	21.1	84.2	20.6	94.2	23.8	98.4	25.5	99.6	26.8
Food	84.0	16.3	115.5	23.1	67.9	16.6	49.1	12.4	45.3	11.7	49.1	13.2
Of which: Rice	(57.6)	(11.2)	(95.1)	(19.0)	(50.5)	(12.3)	(28.7)	(7.2)	(29.9)	(7.7)	(34.2)	(9.2)
Nonfood consumer goods	49.9	9.7	46.0	9.2	40.6	9.9	48.0	12.1	51.6	13.3	42.2	11.4
Energy	107.6	20.9	121.3	24.2	91.9	22.5	96.9	24.5	83.9	21.7	47.0	12.7
Raw material and spare parts	94.3	18.3	97.8	19.6	102.5	25.0	107.6	27.2	107.3	27.8	133.5	35.9
Other (1)	18.3	3.5	13.9	2.8	22.2	5.4	--	--	--	--	--	--
Total imports, c.i.f.	515.8	100.0	500.3	100.0	409.3	100.0	395.8	100.0	386.5	100.0	371.4	100.0
Memorandum items:												
Rice import volume (in thousands of tons)	192.5		351.0		185.1		111.4		106.5		171.6	
Imports, f.o.b. (in millions of SDRs)	433.2		409.0		353.8		343.5		330.7		312.0	

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

(1) Beginning 1984 "other" imports are allocated to the principal import categories.

Table 15

Outstanding Stock of External Debt, 1980-85 (1)
(in millions of SDRs)

	1980		1981		1982		1983		1984		1985	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
Official Creditors	533.3	61.8	824.9	63.2	1,059.6	63.8	1,038.2	57.0	1,152.3	55.3	1,297.1	58.4
Paris Club (2)	(343.4)	(39.8)	(500.0)	(38.3)	(707.6)	(42.6)	(735.1)	(38.7)	(805.8)	(38.7)	(945.3)	(42.5)
Other Countries (3)	(189.9)	(22.0)	(324.9)	(24.9)	(352.0)	(21.2)	(348.2)	(18.3)	(346.5)	(16.6)	(351.8)	(15.8)
International Organizations	218.6	25.3	310.9	23.8	418.9	25.2	487.2	25.7	558.3	26.8	577.5	26.0
IMF	(42.9)	(5.0)	(74.8)	(5.7)	(126.5)	(7.6)	(133.1)	(7.0)	(151.0)	(7.2)	(147.0)	(6.6)
Other oganizations	(175.7)	(20.3)	(236.1)	(18.1)	(292.4)	(17.6)	(354.1)	(18.6)	(407.3)	(19.5)	(430.5)	(19.4)
Banks	101.7	11.8	162.5	12.4	177.0	10.7	184.7	9.7	193.7	9.3	153.9	6.9
Private nonguaranteed	9.0	1.0	7.5	0.6	6.6	0.4	7.2	0.4	21.2	1.0	32.0	1.4
Short-term (4)	--	--	--	--	--	--	41.6	2.2	78.9	3.7	85.2	3.8
Arrears (5)	--	--	--	--	--	--	95.5	5.0	81.4	3.9	77.4	3.5
Total	862.6	100.0	1,305.8	100.0	1,662.1	100.0	1,854.4	100.0	2,085.8	100.0	2,223.1	100.0

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

(1) After debt rescheduling from the Paris Club, from other official creditors , and from commercial banks.
(2) Participating countries are Austria, Belgium, Canada, the Federal Republic of Germany, France, Israel, Italy, Japan, Spain, Sweden, Switzerland, the United Kingdom and the United States.
(3) COMECON, China, and Arab countries; includes exceptional balance of payments financing.
(4) Not available prior to 1984.
(5) Prior to 1983, included in outstanding amounts of principal creditors.

Table 16

External Debt Service Payments, 1986-92 1/

(in millions of SDRs)

	Dec. 1985 outstanding	1986			1987			1988			1989			1990			1991			1992		
		Prin.	Int.	Total	Prin.	Int.	Total	Prin.	Int.	Total	Prin.	Int.	Total	Prin.	Int.	Total	Prin.	Int.	Total	Prin.	Int.	Total
Official creditors	1,297.1	13.3	49.3	62.6	16.5	65.1	81.6	115.0	114.0	229.0	132.5	106.3	238.8	145.8	94.6	240.4	149.3	83.2	232.5	185.1	71.8	256.9
Paris Club	(945.3)	(3.4)	(41.1)	(44.5)	(0.4)	(53.3)	(53.7)	(68.5)	(79.4)	(147.9)	(80.6)	(75.3)	(155.9)	(89.4)	(67.6)	(157.0)	(103.4)	(60.4)	(163.8)	(123.4)	(52.9)	(176.3)
Other	(351.8)	(9.9)	(8.2)	(18.1)	(16.1)	(11.8)	(27.9)	(46.5)	(34.6)	(81.1)	(51.9)	(31.0)	(82.9)	(56.4)	(27.0)	(83.4)	(45.9)	(22.8)	(68.7)	(61.7)	(18.9)	(80.6)
International Organizations	577.5	58.0	18.7	76.7	44.8	17.4	62.2	47.7	17.8	65.5	57.2	17.8	75.0	54.5	17.4	71.9	40.7	17.6	58.3	26.3	16.2	42.5
IMF	(147.0)	(45.2)	(13.0)	(58.2)	(32.2)	(11.0)	(43.2)	(34.1)	(10.3)	(44.4)	(41.2)	(8.5)	(49.7)	(37.7)	(6.0)	(43.7)	(24.8)	(3.9)	(28.7)	(10.0)	(2.6)	(12.6)
Other	(430.5)	(12.8)	95.7)	(18.5)	(12.6)	(6.4)	(19.0)	(13.6)	(7.5)	(21.1)	(16.0)	(9.3)	(25.3)	(16.8)	(11.4)	(28.2)	(15.9)	(13.7)	(29.6)	(16.3)	(13.6)	(29.9)
Banks	153.9	17.9	12.7	30.6	18.6	10.9	29.5	18.7	9.3	28.0	23.8	7.5	31.3	23.8	5.4	29.2	21.3	3.3	24.6	21.3	1.4	22.7
Other private	32.0	9.2	2.3	11.5	7.6	1.9	9.5	6.6	1.7	8.3	3.0	1.6	4.6	3.0	0.9	3.9	2.9	0.7	3.6	2.9	0.6	3.5
Short-term	85.2	7.6 2/	10.3	17.9	22.4 3/	6.0	28.4	27.0 3/	6.0	33.0	—	6.0	6.0	—	6.0	6.0	—	6.0	6.0	—	6.0	6.0
Arrears	77.4	8.0	—	8.0	8.0	—	8.0	18.0	—	18.0	20.0	—	20.0	10.0	—	10.0	10.0	—	10.0	8.0	—	8.0
Total	2,223.1	114.0	93.3	207.3	117.9	101.3	219.2	233.0	148.8	381.8	236.5	139.2	375.7	237.1	124.3	365.4	224.2	110.8	335.0	243.6	96.0	339.6

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

1/ After rescheduling under Paris Club V (October 1986) and pari passu rescheduling with other official creditors through December 31, 1987, and after rescheduling with commercial banks in October 1984 and in December 1985, and with the U.S.S.R. of petroleum financing due in 1986.

2/ Relates to 20 percent down payment (nonrescheduled portion) of the U.S.S.R.'s petroleum financing.

3/ Relates to the repayment of 70 percent of previous year's petroleum imports financed by the U.S.S.R.

Table 17

Balance of payments, 1981-86

(in millions of SDRs)

	1981	1982	1983	1984	1985	1986 Proj.
Exports, f.o.b.	281.5	296.4	289.7	325.2	274.5	286.2
Imports, f.o.b.	-433.2	-409.0	-353.8	-343.5	-330.7	-312.0
Trade balance	-151.7	-112.6	-64.1	-18.3	-56.2	-25.8
Service receipts	55.6	49.7	45.0	56.9	62.0	74.3
Service payments	-267.9	-272.7	-268.0	-289.2	-296.0	-317.5
Freight	-66.2	-68.1	-49.6	-48.1	-46.1	-43.7
Transport and travel	-59.3	-55.7	-54.6	-61.8	-68.9	-64.5
Investment income	-78.3	-91.4	-106.6	-134.9	-131.2	-150.7
Other	-63.7	-57.5	-57.2	-44.4	-49.8	-58.6
Services, net	-211.9	-223.0	-223.0	-232.3	-234.0	-243.2
Of which: interest (including moratorium interest on rescheduled debt)	(-75.1)	(-88.2)	(-104.4)	(-133.2)	(-129.7)	(-149.3)
Private unrequited transfers	3.4	-1.3	-1.1	9.3	37.4	28.5
Current account	-360.2	-336.9	-288.2	-241.3	-252.8	-240.5
Public unrequited transfers	53.1	65.5	56.9	66.1	59.4	87.9
Nonmonetary capital (net)	237.7	109.9	184.1	179.5	162.3	181.6
Drawings	277.2	190.1	181.1	117.9	143.4	168.4
Amortization 1/	-93.2	-164.2	-183.1	-127.0	-147.0	-136.0
Debt relief (net of down payments)	53.7	84.0	186.1	164.9	151.7	164.7 2/
Official creditors	(50.3)	(82.1)	(125.1)	(141.1)	(137.9)	(164.7)
Commercial Banks 3/	(3.4)	(1.9)	(61.0)	(23.8)	(13.8)	(—)
Petroleum financing	...	...	...	23.7	14.2	-15.5
Drawing				(23.7)	(37.9)	(22.4)
Amortization				(—)	(-23.7)	(-37.9)
National Banks (net)	-18.1	-23.8	-0.3	-12.2	1.0	--
Other 4/	5.3	77.6	-41.7	23.6	22.3	--
Overall balance	-82.2	-107.7	-89.2	15.7	-7.8	29.0
Financing	82.2	107.7	89.2	-15.7	7.8	-29.0
IMF (net)	31.6	51.7	6.5	17.9	-3.4	3.4
Purchases	39.0	52.4	10.2	41.4	29.0	44.2
Repurchases	-7.4	-0.7	-3.7	-23.5	-32.4	-40.8
Net cash change in arrears (decrease -) 5/	59.0	63.8	69.6	-9.0	-8.3	-8.0
Net central bank reserves (increase -) 5/	-8.4	-7.8	13.1	-24.6	19.5	-24.4
Financing gap	--	--	--	--	--	--
Memorandum items:						
Current account deficit as percent of GDP 6/	-14.6	-13.1	-10.9	-10.4	-11.0	-10.4
Outstanding arrears 5/	...	...	95.5	81.4	77.4	69.4
Freely available reserves	...	...	7.7	15.2	12.9	26.0
Debt service ratio before rescheduling 7/	45.9	72.9	87.0	75.6	93.4	95.5
Debt service ratio after rescheduling 8/	34.0	48.9	31.4	33.4	49.2	51.3
GDP	2,463.0	2,580.0	2,665.0	2,315.5	2,308.2	2,302.0
FMG/SDR exchange rate	320.4	386.1	459.9	590.8	672.6	798.6

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

1/ Before current year's debt rescheduling.
2/ After debt relief obtained from Paris Club V (October 1986) and from other official creditors on comparable terms.
3/ Includes small amount of debt relief from private creditors other than commercial banks. In December 1985 commercial banks rephased amortization payments on previously rescheduled debt through 1992. The impact of this debt relief in 1986 has been taken into account by reducing scheduled amortization payments.
4/ Includes valuation of adjustment, short-term capital other than petroleum financing, errors and omissions, and SDR 3.5 million in SDR allocations in 1981.
5/ Series not comparable prior to 1983 since central bank foreign liabilities have been revalued at appropriate exchange rates only beginning mid-1983.
6/ The high current account/GDP ratio reflects, in part, the impact of the depreciation of the exchange rate of the Malagasy franc on GDP expressed in terms of SDRs.
7/ Includes impact of previous year's rescheduling, but excludes that of the current year.
8/ Includes impact of reschedulings through the current year.

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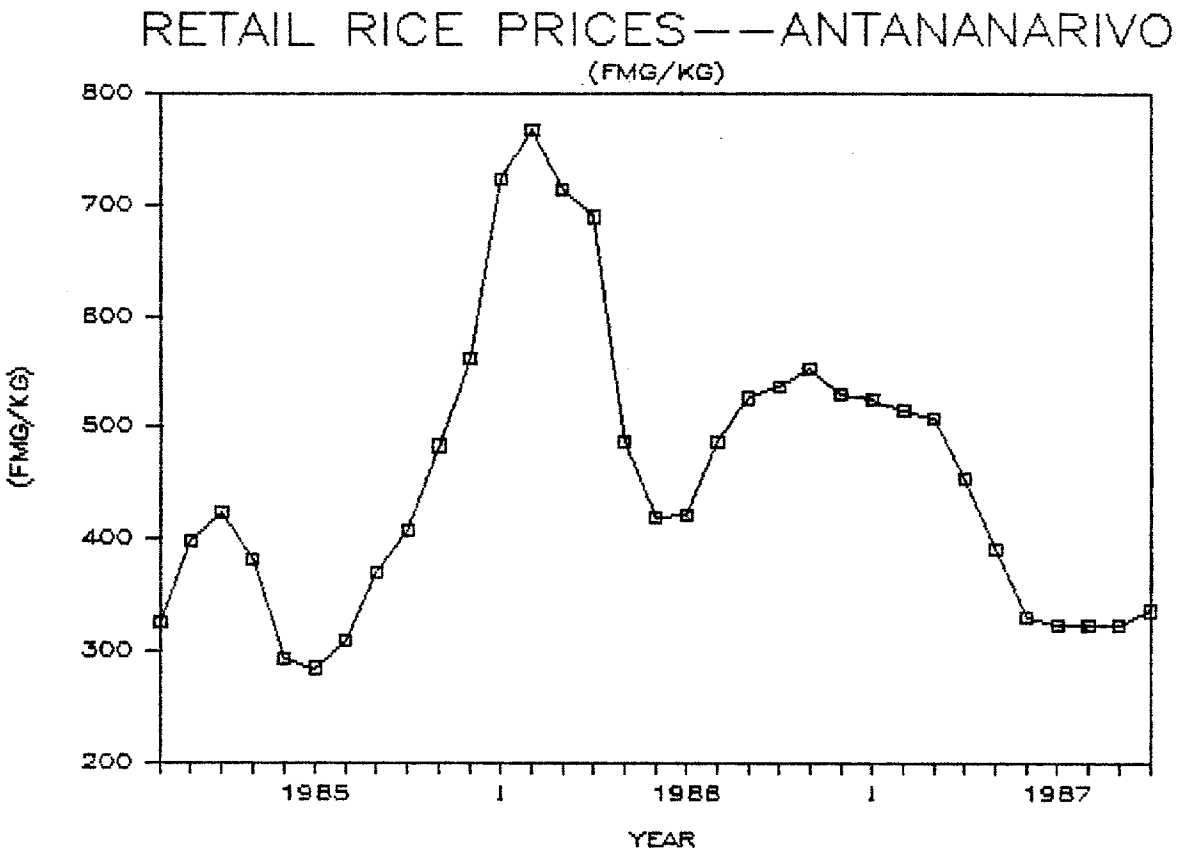
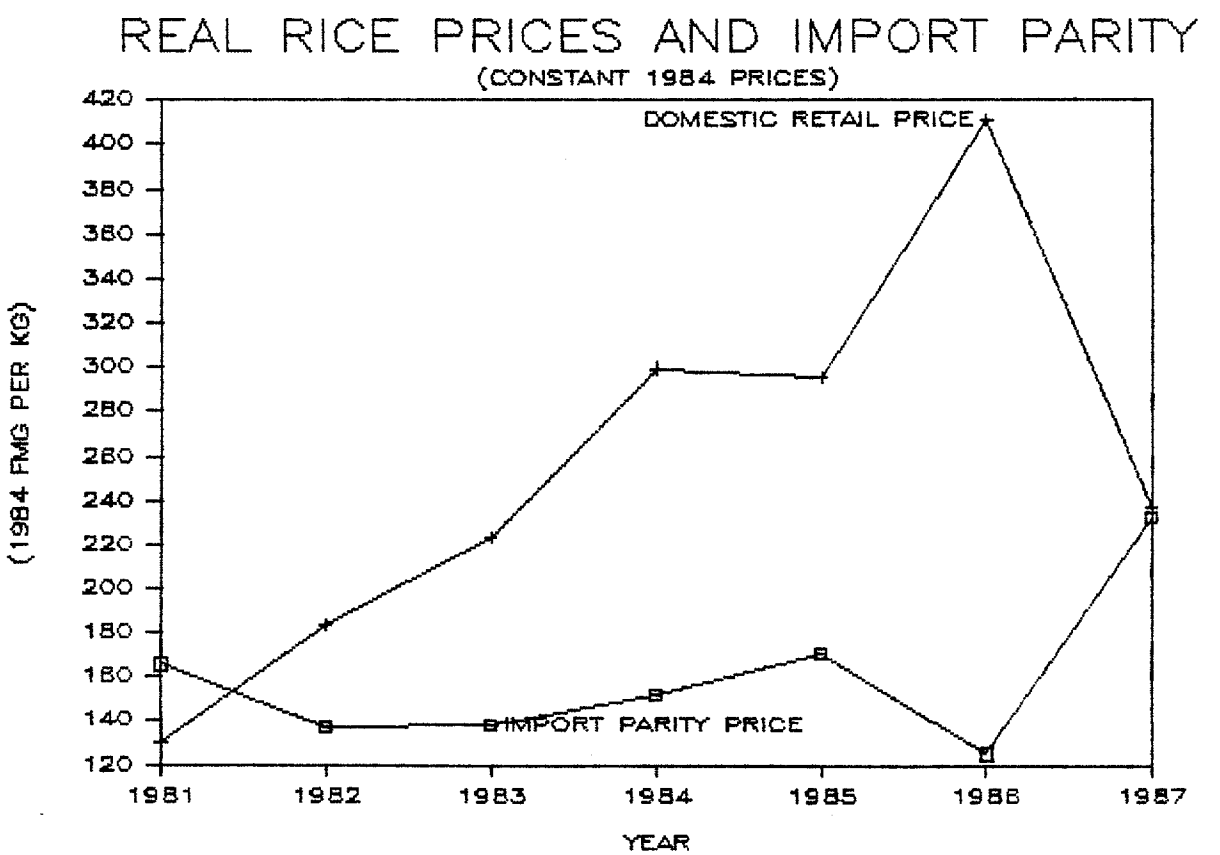
Graph 1



Graph 2



ANNEX B

INITIAL ENVIRONMENTAL EXAMINATION

Project Country: Madagascar

Project Title: Madagascar Economic Policy Reform Program

Funding: $17 million FY: 1988

IEE Prepared by: Donna Stauffer, Project Development Officer

Environmental Action Recommended: Categorical Exclusion

Discussion: The proposed Madagascar Economic Policy Reform Program meets the criteria for Categorical Exclusion under Section 216.2(c) of Regulation 16. A cash grant of $15.0 million will be provided to support the Government of Madagascar's reform of the foreign exchange allocation system and will be used to finance imports under an open general licensing system. The use of cash grant funds is not tied to either specific commodities or a specifically identifiable project and thus may be considered as an "Action which does not have an effect on the natural or physical environment". This, according to Section 216.2(c)(1)(i), is a criterion for categorical exclusion. The balance of program funding, $2.0 million, will be used to finance technical services, studies and training in support of policy reform measures. This portion of the grant meets the criteria for categorical exclusion provided in Section 216.2(c)(2)(xiv).

Concurrence: _____
Samuel S. Rea, A.I.D. Representative

Bureau Environmental Officer's Decision:

Approved: _____

Disapproved: _____

Date: _____

Clearance: GC/AFR _____ Date: _____