

# EUROPEAN ECONOMY

EUROPEAN COMMISSION  
DIRECTORATE-GENERAL FOR ECONOMIC AND FINANCIAL AFFAIRS



REPORTS AND STUDIES

**REPORT ON THE IMPLEMENTATION  
OF MACRO-FINANCIAL ASSISTANCE  
TO THIRD COUNTRIES IN 1994**



*European Economy* appears twice a year. It contains important reports and communications from the Commission to the Council and the Parliament on the economic situation and developments. As a complement to *European Economy*, the series *Reports and studies* will be published on problems concerning economic policy.

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**European Commission**

# **EUROPEAN ECONOMY**

**Reports and studies**

**Directorate-General for Economic and Financial Affairs**

**1995**

**Number 2**





# **Report on the implementation of macro-financial assistance to third countries in 1994**

**Communication from the Commission  
to the Council and the European Parliament**

## Abbreviations and symbols used

### *Member States*

B	Belgium
DK	Denmark
D	Germany
WD	West Germany
GR	Greece
E	Spain
F	France
IRL	Ireland
I	Italy
L	Luxembourg
NL	The Netherlands
AT	Austria
P	Portugal
FI	Finland
SE	Sweden
UK	United Kingdom
EUR 9	European Community excluding Greece, Spain and Portugal
EUR 10	European Community excluding Spain and Portugal
EUR 12–	European Community, 12 Member States including West Germany
EUR 12+	European Community, 12 Member States including Germany
EUR 15	European Community, 15 Member States
EUR 15+	European Community, 15 Member States including West Germany

### *Currencies*

ECU	European currency unit
BFR	Belgian franc
DKR	Danish crown (krone)
DM	German mark (Deutschmark)
DR	Greek drachma
ESC	Portuguese escudo
FF	French franc
HFL	Dutch guilder
IRL	Irish pound (punt)
LFR	Luxembourg franc
LIT	Italian lira
PTA	Spanish peseta
UKL	Pound sterling
USD	US dollar
SFR	Swiss franc
YEN	Japanese yen
CAD	Canadian dollar
ÖS	Austrian schilling
R	Russian rouble
ROL	Romanian leu
SKK	Slovak crown



### *Other abbreviations*

ACPs	African, Caribbean and Pacific countries having signed the Lomé Convention
ECSC	European Coal and Steel Community
EDF	European Development Fund
EIB	European Investment Bank
EMCF	European Monetary Cooperation Fund
EMS	European Monetary System
ERDF	European Regional Development Fund
Euratom	European Atomic Energy Community
Eurostat	Statistical Office of the European Communities
GDP (GNP)	Gross domestic (national) product
GFCF	Gross fixed capital formation
LDCs	Less-developed countries
Mio	Million
Mrd	1 000 million
NCI	New Community Instrument
OCTs	Overseas countries and territories
OECD	Organization for Economic Cooperation and Development
OPEC	Organization of Petroleum Exporting Countries
PPS	Purchasing power standard
SMEs	Small and medium-sized enterprises
toe	Tonne of oil equivalent
:	Not available





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# I — Overview

## 1. Introduction

Initially conceived for intra-Community balance-of-payments support, macro-financial assistance from the Community has been extended since 1990 to third countries, mainly those of Central and Eastern Europe, with a view to supporting their political and economic reform efforts. As they embarked on their process of transition to a market economy, the countries of this region were faced with similar problems:

- (i) The costs attached to the first steps of reform, liberalization and stabilization, were substantial; in particular: commitment to unify the exchange markets and make the national currency convertible for current-account transactions at an early stage of the reform process required raising the level of the international reserves of those countries; and some countries were also overburdened by a sizeable public debt inherited from the previous regime.
- (ii) In addition to the needs relating to the transition efforts, the Central and East European countries (CEECs) faced additional external shocks: the consequences of the Gulf War, including the embargo which had particularly severe effects in economies such as Bulgaria; the dramatic collapse of the Council for Mutual Economic Assistance (Comecon) trading system, which had been based on State-directed flows of goods at artificial prices; and later, the effect of the trade embargo on Serbia-Montenegro.
- (iii) The sums available from the international financial institutions (IFIs) — mostly the International Monetary Fund (IMF) and the World Bank — were insufficient.
- (iv) Flows from the private sector were virtually non-existent because of the relative unfamiliarity with the economies concerned and the great uncertainties surrounding the first stages of the reform and transition process.

Against this background, the European Community decided to extend macro-financial assistance to the countries in the region in complement to the financing provided by the IFIs. It was also decided that, in the context of the assistance coordination process agreed among the 24 industrial countries (G24) to help the CEECs, the Commission should get other donors to contribute in a similar way to support the economic programmes that these countries were implementing in agreement with the IMF and World Bank.

In early 1991, at the initiative of the European Commission, a set of principles was agreed among the G24 that have since served as guidelines for EU/G24 macro-financial assistance; accordingly, the operations have conformed with the following principles:<sup>1</sup>

- (i) *Exceptional character*: all operations are undertaken on a strictly case-by-case basis. The operations are to be discontinued when the recipient country can fully rely on financing from the IFIs and private sources of capital.
- (ii) *Complementarity*: the basic prerequisite for the mobilization of the assistance is the existence of a significant residual external financing gap over and above the resources provided by the IMF and other multilateral institutions and despite the implementation of strong economic stabilization and reform programmes.
- (iii) *Conditionality*: the assistance is generally released in successive tranches, the disbursement of each being conditional upon the fulfilment of macroeconomic performance and structural adjustment criteria, consistent with the economic programmes agreed between the beneficiary countries and the IMF.

A number of such support operations by the European Union and the G24 took place during the period 1990-93 covering most Central and East European countries eligible for G24 assistance (Table 1):

- (i) The first Community macro-financial operation for a third country dates back to February 1990, when the Council decided to provide Hungary with a five-year ECU 870 million loan facility in support of the country's efforts to overcome structural adjustment difficulties in the context of an IMF stand-by arrangement.
- (ii) In 1991, the Council adopted four new Decisions granting financial assistance to CEECs totalling ECU 1 220 million: ECU 375 million for Czechoslovakia; ECU 290 million for Bulgaria; ECU 375 million for Romania and a further ECU 180 million for Hungary.<sup>2</sup>
- (iii) In late 1992, another series of Community operations was decided by the Council for CEECs, amounting to ECU 480 million, comprising a further ECU 110 million loan for Bulgaria, a further ECU 80 million loan for Romania; an ECU 220 million loan to the Baltic States (40 million for Estonia, 80 million for Latvia and 100 million for Lithuania), and a grant of ECU 70 million to Albania.<sup>3,4</sup>

<sup>2</sup> See: Report on the implementation of medium-term financial assistance to the balances of payments of Central and East European countries, COM(92) 400, 16.9.1992.

<sup>3</sup> There were no new operations in 1993.

<sup>4</sup> See: Report on the implementation of macro-financial assistance to third countries, COM(94) 229, 7.6.1994.

<sup>1</sup> These principles were recently reconfirmed by the Council.

**Table 1**

**Community macro-financial assistance to third countries extended through end-1994**  
**(status of effective disbursements as of June 1995)**

<i>(million ECU)</i>					
Country	Maximum amount authorized	Date of Council Decision	Disbursed	Amounts and dates of disbursements	Undisbursed
<b>A — Macro-financial assistance to CEECs</b>					
Hungary I	870	22.2.1990	610	350 — April 1990 260 — February 1991	260
Czech and Slovak Federal Republic	375	25.2.1991	375	185 — mid-1991 190 — February 1992	—
Hungary II	180	24.6.1991	180	100 — August 1991 80 — January 1993	—
Bulgaria I	290	24.6.1991	290	150 — August 1991 140 — March 1992	—
Romania I	375	22.7.1991	375	190 — January 1992 185 — April 1992	—
Albania I	70	28.9.1992	70	35 — December 1992 35 — August 1993	—
Baltics States	220	23.11.1992	110		110
of which:					
Estonia	40		20	March 1993	20
Latvia	80		40	March 1993	40
Lithuania	100		50	July 1993	50
Romania II	80	27.11.1992	80	February 1993	—
Bulgaria II	110	19.10.1992	70	December 1994	40
Romania III	125	20.6.1994	—	—	125
Albania II	35	28.11.1994	15	June 1995	20
Slovakia	130	22.12.1994	—	—	130
Total A	2 860		2 175		685
<b>B — Macro-financial assistance to other third countries</b>					
Israel	160	22.7.1991	160	March 1992	—
Algeria I	400	23.9.1991	400	250 — January 1992 150 — August 1994	—
Moldova	45	13.6.1994	25	25 — December 1994	20
Algeria II	200	22.12.1994	—	—	200
Ukraine	85	22.12.1994	—	—	85
Total B	890		585		305
Total A + B	3 750		2 760		990

Outside the region of Central and Eastern Europe, two other Community loan operations were decided by the Council in 1991. In the context of Community support for Mediterranean countries adversely affected by the Gulf conflict, the Council made an ECU 160 million soft loan available to Israel in July 1991. In September 1991, a medium-term loan of ECU 400 million was also decided in favour of Algeria to help the country carry through the political and economic reforms under way.<sup>1</sup>

## 2. Macro-financial assistance in 1994

In 1994, Community macro-financial assistance was provided to a series of countries in Central and Eastern Europe, the European new independent States (NISs) of the former Soviet Union, and the Mediterranean area, in a total amount of ECU 620 million (Table 1).

New operations in favour of CEECs comprised a further loan of up to ECU 125 million for Romania, a further grant of up to ECU 35 million for Albania, and a loan of up to ECU 130 million for Slovakia. Furthermore, the loan to Bulgaria, which had been decided in 1992, but could not be disbursed owing to bad macroeconomic performance in 1993, was reactivated in 1994 in the context of a new economic programme. As in the previous years, all these initiatives were taken in the context of G24 financing packages complementing resources provided by the IFIs. Overall, the requests for exceptional financial assistance from the G24 totalled USD 977 million, of which the Community contributed approximately half (bringing cumulative requests for G24 assistance to USD 4.3 billion since 1991 — Table 2).

Operations in favour of European NISs comprised a loan of up to ECU 45 million for Moldova, and of up to ECU 85 million for Ukraine. These initiatives were taken in the context of exceptional international assistance coordinated by the World Bank, that mobilized respectively USD 130 million, and USD 185 million of new financing to complement resources by the IFIs. In the case of Ukraine, Russia and Turkmenistan also provided substantial bilateral contributions through restructuring of their claims.

With respect to the Mediterranean region, the loan to Algeria (ECU 400 million), decided in 1991, was reactivated in 1994 in the context of a new economic programme supported by the IMF; and the second tranche (ECU 150 million) was disbursed. In the same context, a further loan to Algeria for an amount of up to ECU 200 million was decided in late 1994. Again, these initiatives were part of an international concerted effort to provide exceptional complementary assistance, that involved

bilateral contributions of new financing as well as debt-restructuring operations from Paris Club and London Club creditors.

Each Community operation has continued to respond to the set of principles established in 1991. In particular, EU macro-financial assistance has supported efforts by recipient countries to bring about economic reforms and structural changes. In close coordination with the IMF and the World Bank, it has promoted policies tailored to the specific national needs, designed to stabilize the financial situation and set up market-oriented economies (macroeconomic performance and progress in reforms in beneficiary countries are summarized in Tables 4 and 5 and discussed country by country in the following chapters).

### Towards a more policy-oriented approach

With the large geographical scope of macro-financial assistance operations initiated in 1994, the economic conditions among beneficiaries have shown a great diversity. However, beyond these differences, the EU macro-financial instrument has evolved significantly. In particular, in the case of the CEECs:

- (i) Macro-financial support has been part of a much broader effort by the European Union to smooth the transition process in Central and Eastern Europe and to establish closer links with its neighbouring countries. The framework for that effort has been further clarified; in particular, Association Agreements were signed during the period 1991-95 with most of these countries. Moreover, in June 1993, a decisive step was taken at Copenhagen, when the European Council accepted the goal of EU membership for those associated countries and put forward political and economic measures to create more favourable conditions to this end. Macro-financial assistance, the possible use of which was explicitly mentioned in the chapter on financial cooperation of the Association Agreements, was therefore to be seen in the context of a long-term partnership with the associated countries. The Essen European Council of December 1994 confirmed the conclusions of the European Councils in Copenhagen and Corfu that the associated States of Central and Eastern Europe can become members of the European Union if they so desire and as soon as they are able to fulfil the necessary conditions. It has decided to boost and improve the process of further preparing the associated States of Central and Eastern Europe.
- (ii) The achievement of a successful transition towards a market economy increasingly appeared as a complex protracted process. More specifically, the necessary links between macroeconomic stabilization and structural adjustment (and the need to put more emphasis on

<sup>1</sup> See: Report on the implementation of macro-financial assistance to third countries, COM(94) 229, 7.6.1994.

**Table 2**

**EU/G24 macro-financial assistance to Central and Eastern Europe since 1991 (cumulative amounts)**  
**(status as of December 1994)**

Country (Identified gaps)	Albania (USD 237 million)					Baltic States (USD 600 million)					Bulgaria (USD 1 130 million)				
	Commitments			Disbursements		Commitments			Disbursements		Commitments			Disbursements	
	Million USD	% of gap	% of commit- ments	Million USD	% of disbur- sements	Million USD	% of gap	% of commit- ments	Million USD	% of disbur- sements	Million USD	% of gap	% of commit- ments	Million USD	% of disbur- sements
European Community	123,5	52,1	77,4	100,1	88,7	300,0	50,0	57,4	150,0	52,3	533,3	47,2	64,4	487,7	75,0
EFTA	16,0	6,8	10,0	4,2	3,7	123,1	20,5	23,5	66,3	23,1	126,0	11,2	15,2	95,0	14,6
of which:															
AT, FI, SE	13,5	5,7	8,5	4,2	3,7	81	13,5	15,5	66,3	23,1	69	6,1	8,3	50	7,7
USA	—	—	—	—	—	—	—	—	—	—	10,0	0,9	1,2	10,0	1,5
Japan	20,0	8,4	12,5	8,5	7,5	100,0	16,7	19,1	70,4	24,6	150,0	13,3	18,1	58,0	8,9
Others	—	—	—	—	—	—	—	—	—	—	8,7	0,8	1,1	—	—
Total	159,5	67,3	100,0	112,8	100,0	523,1	87,2	100,0	286,7	100,0	828	73,3	100,0	650,7	100,0

Country (Identified gaps)	Czech and Slovak Federal Republic (USD 1 000 million)					Hungary <sup>1</sup> (USD 500 million)					Romania (USD 1 455 million)				
	Commitments			Disbursements		Commitments			Disbursements		Commitments			Disbursements	
	Million USD	% of gap	% of commit- ments	Million USD	% of disbur- sements	Million USD	% of gap	% of commit- ments	Million USD	% of disbur- sements	Million USD	% of gap	% of commit- ments	Million USD	% of disbur- sements
European Community	500,0	50,0	56,4	500,0	58,0	250,0	50,0	48,3	250,0	50,7	740,6	50,9	68,9	597,9	69,8
EFTA	146,0	14,6	16,5	146,0	16,9	95,0	19,0	18,3	95,0	19,3	162,2	11,1	15,1	136,4	15,9
of which:															
AT, FI, SE	90,0	9,0	10,1	90,0	10,4	50	10,0	9,7	50	10,1	87,3	6,0	8,1	71,5	8,3
USA	15,0	1,5	1,7	15,0	1,7	10,0	2,0	1,9	10,0	2,0	—	—	—	—	—
Japan	200,0	20,0	22,5	200,0	23,2	150,0	30,0	29,0	125,0	25,4	150,0	10,3	14,0	100,0	11,7
Others	26,0	2,6	2,9	1,0	0,1	12,8	2,6	2,5	12,8	2,6	22,0	1,5	2,0	22,0	2,6
Total	887,0	88,7	100,0	862,0	100,0	517,8	103,6	100,0	492,8	100,0	1 074,8	73,9	100,0	856,3	100,0

Country (Identified gaps)	Slovakia (USD 300 million)				Total (USD 5 222 million)					
	Commitments		Disbursements		Commitments		Disbursements			
	Million USD	% of gap	% of commit- ments	Million USD	% of disbur- sements	Million USD	% of gap	% of commit- ments	Million USD	% of disbur- sements
European Community	156,0	52,0	64,1	0,0	0,0	2 603,5	49,9	61,5	2 085,7	64,0
EFTA	27,4	9,1	11,2	0,0	0,0	695,6	13,3	16,4	542,9	16,6
of which:										
AT, FI, SE	16,4	5,5	6,7	—	—	407,1	7,8	9,6	332,0	10,2
USA	—	—	—	—	—	35,0	0,7	0,8	35,0	1,1
Japan	60,0	20,0	24,7	0,0	0,0	830,0	15,9	19,6	561,9	17,2
Others	—	—	—	—	—	69,5	1,3	1,6	35,8	1,1
Total	243,4	81,1	100,0	0,0	0,0	4 233,6	81,1	100,0	3 261,3	100,0

<sup>1</sup> In 1990, the Community committed an additional ECU 870 million loan in favour of Hungary which is not taken into consideration in this table since it took place outside the G24 process.

Source: European Commission.

structural reforms) became more obvious. For the IMF, it translated into a better integration of those aspects into the programmes that were negotiated with the authorities of those countries. In parallel, the World Bank helped the authorities to design specific programmes, centred around key reforms in the enterprise and financial sectors, to be supported by policy-based lending operations with conditionality relating to progress with structural reform.

From the European Union's point of view, all this has affected the timing and content of the programmes. EU lending has evolved towards a more policy-oriented role and a greater synergy has been achieved with grant-based EU instruments (mostly the EU PHARE — Poland and Hungary: aid for economic restructuring — programme). This can be illustrated by the operations initiated in 1994 with Bulgaria, Romania and Slovakia.

Macroeconomic imbalances persisted and reform remained elusive in Bulgaria and Romania throughout 1993. Arrangements concluded in 1992 with the IMF and the World Bank ran off-track, and discussions on new comprehensive programmes dragged on during most of 1993. At the same time, the newly independent Slovakia was experiencing difficulties coping with the huge loss of transfers that it had received under the Federation. For these countries, therefore, it was important that financial assistance be available when a renewed willingness to progress with stabilization and reform emerged. This happened from late 1993 to early 1994 when authorities in all three countries decided to engage in new comprehensive programmes that could be supported by the international community. The European Union decided at this juncture to respond favourably to the request for further macro-financial assistance in the context of the G24 to complement IMF and World Bank arrangements.

Although the total amounts of resources committed by the G24 have not been, in relative terms, as large as in the previous operations, the coordination between the Commission and the Bretton Woods institutions has been more intense. In addition, the policy dialogue with the authorities in the countries concerned has broadened considerably.

The dialogue established with the authorities in the framework of macro-financial assistance involved a two-stage process.

- (i) In the first stage, the main objective was to concur in the rapid implementation of key policy measures at the outset of the programme.
- (ii) In the second stage, the main objective was to assess the government's strategy for structural reform. Two major fields of investigation were the privatization process and the restructuring of the public enterprise sector. In parallel,

discussions were held with EU PHARE services with a view to finding appropriate ways to strengthen the capacity of the relevant national institutions to handle these tasks.

In both areas of stabilization and structural reform, policies have been monitored in close cooperation with the IMF and the World Bank.

Macro-financial assistance to countries other than associated CEECs has also evolved, although to a lesser degree. Operations could not be embedded in a context of long-term partnership similar to that with associated countries; however, more emphasis has also been put on structural reforms. In the case of Moldova and Ukraine, where macro-financial assistance initiated in 1994 has been supporting efforts at an early stage of the transition to market economies, these have included the introduction of a necessary legislative framework as well as the implementation of important structural reform, in particular in the key areas of liberalization of foreign trade, introduction of convertibility and price liberalization (that were started to be put in place at the beginning of the decade in most associated CEECs).

In Albania, where the first stage of economic stabilization and reform had been successfully achieved, assistance has been supporting the shift by the Albanian authorities from a mainly short-term horizon, that had been dictated by the state of crisis, towards a consistent medium-term approach in the framework of a comprehensive medium-term economic programme. In Algeria, resumption of assistance by the European Union has been supporting renewed efforts towards the establishment of a convertible market-based exchange rate, the liberalization of trade and prices, and the tightening of financial discipline for the State-owned enterprises.

## Burden-sharing

While EU macro-financial assistance has been evolving towards a deepened policy-oriented approach, resources mobilized by the Union in this context have been decreasing substantially (Tables 3 and 3.1). Initially, an important feature of EU assistance was that very large sums of money were to be found to support Bretton Woods institution programmes. The European Union played a key role both as the largest single provider of these funds, (mobilizing 54% of total balance-of-payments support to Hungary in 1990) and through its role as the coordinator of bilateral assistance (the G24 process for CEECs since 1991), which ensured a wide participation in this effort.

Eventually, more resources were mobilized by the IFIs (whose contribution increased from 21% of balance-of-payments support — excluding debt relief — in 1991 to some 70%



in 1994): a new lending instrument, the systemic transformation facility (STF) was created which, together with the increase in the access limits, enabled the IMF to increase its assistance to CEECs and countries of the former Soviet Union. The World Bank, for its part, developed successive generations of policy-based balance-of-payments operations (structural adjustment loans — SALs — followed by financial and enterprise and financial sectors adjustment loans — EFSALs<sup>1</sup>).

In parallel, contributions by external creditors, both public and private, were mobilized in the framework of debt-relief and debt-reduction operations (Algeria, Bulgaria, Ukraine), accounting for a substantial share of balance-of-payments support in 1991 and 1994.

In this context, relative contributions<sup>2</sup> from the European Union and from other bilaterals (beyond debt-relief operations) declined sharply from 54 and 25%, respectively, in 1990 to 17 and 12%, respectively, in 1994 (or 6 and 5%, respectively, of total commitments including debt-relief operations).

**Table 3**

**Balance-of-payments support to recipients of EU macro-financial assistance by contributor, 1990-94<sup>1</sup>**

	<i>(% of total commitments)</i>			
	1990	1991	1992	1994
<i>Including debt relief</i>				
<b>IFIs</b>	21	50	69	27
IMF	11	37	40	21
World Bank	10	13	29	6
<b>Bilaterals</b>	79	50	31	73
EU <sup>2</sup>	54	20	19	6
Other bilaterals <sup>3</sup>	25	13	13	5
of which:				
USA	0	0	0	1
Japan	10	8	5	2
Debt relief	0	18	0	63
Paris Club	—	5	—	32
London Club	—	—	—	28
Other <sup>4</sup>	—	13	—	2
<i>Excluding debt relief</i>				
<b>IFIs</b>	21	61	69	71
IMF	11	45	40	56
World Bank	10	16	29	15
<b>Bilaterals</b>	79	39	31	29
EU <sup>2</sup>	54	24	19	17
Other bilaterals <sup>3</sup>	25	15	13	12
of which:				
USA	0	0	0	2
Japan	10	9	5	6

<sup>1</sup> Based on Council Decisions for EU operations. No operation was decided in 1993.

<sup>2</sup> EU macro-financial assistance.

<sup>3</sup> Including EU Member States.

<sup>4</sup> Syndicated commercial banks' loan in favour of Algeria in 1991, debt relief in favour of Ukraine by Russia and Turkmenistan in 1994.

<sup>1</sup> Most EFSAL operations discussed with beneficiary countries could not be concluded by end-1994 and are therefore not included in the commitments recorded in Tables 3 and 3.1. When they are, contributions by the World Bank will increase accordingly.

<sup>2</sup> Only the countries for which macro-financial assistance from the European Union has been mobilized are covered by these statistics.

**Table 3.1**

**Balance-of-payments support to recipients of EU macro-financial assistance by contributor, 1990-94**  
(million USD and % of total commitments and disbursements)

Balance-of-payments support — 1990								
	Total		Disbursements		Hungary I		Disbursements	
	Commitments	%	Commitments	%	Commitments	%	Commitments	%
	Million USD		Million USD		Million USD		Million USD	
IFIs	419	21	375	23	419	21	375	23
IMF	219	11	175	11	219	11	175	11
World Bank (policy-based)	200	10	200	12	200	10	200	12
<b>Bilaterals</b>	1 618	79	1 288	77	1 618	79	1 288	77
European Union	1 108	54	777	47	1 108	54	777	47
USA	0	0	0	0	0	0	0	0
Japan	200	10	200	12	200	10	200	12
Germany	311	15	311	19	311	15	311	19
Other bilaterals	—	0	—	0	0	0	0	0
<b>Total</b>	2 037	100	1 663	100	2 037	100	1 663	100

Balance-of-payments support — 1991												
	Total		Disbursements		Algeria I		Disbursements		Bulgaria I		Disbursements	
	Commitments	%	Commitments	%	Commitments	%	Commitments	%	Commitments	%	Commitments	%
	Million USD		Million USD		Million USD		Million USD		Million USD		Million USD	
IFIs	5 607	50	3 930	43	690	23	443	19	640	35	540	33
IMF	4 177	37	2 825	31	390	13	293	12	390	22	390	24
World Bank (policy-based)	1 430	13	1 105	12	300	10	150	6	250	14	150	9
<b>Bilaterals</b>	5 600	50	5 147	57	2 290	77	1 938	81	1 168	65	1 117	67
European Union	2 190	20	1 988	22	540	18	338	14	400	22	400	24
USA	35	0	35	0	0	0	0	0	10	1	10	1
Japan	850	8	633	7	300	10	150	6	100	6	58	4
Other bilaterals	521	5	487	5	0	0	0	0	104	6	95	6
Debt relief	2 004	18	2 004	22	1 450	49	1 450	61	554	31	554	33
Paris Club	554	5	554	6	—	—	—	—	554	31	554	33
Syndicated loan	1 450	13	1 450	16	1 450	49	1 450	61	—	—	—	—
<b>Total</b>	11 207	100	9 077	100	2 980	100	2 381	100	1 808	100	1 657	100

	Czech and Slovak		Federal Republic		Hungary		Disbursements		Romania I		Disbursements	
	Commitments	%	Commitments	%	Commitments	%	Commitments	%	Commitments	%	Commitments	%
	Million USD		Million USD		Million USD		Million USD		Million USD		Million USD	
IFIs	1 302	59	1 302	60	2 262	81	1 020	67	713	49	625	46
IMF	852	39	852	39	2 012	72	845	56	533	37	445	33
World Bank (policy-based)	450	21	450	21	250	9	175	12	180	12	180	13
<b>Bilaterals</b>	887	41	862	40	518	19	493	33	737	51	737	54
European Union	500	23	500	23	250	9	250	17	500	34	500	37
USA	15	1	15	1	10	0	10	1	—	—	—	—
Japan	200	9	200	9	150	5	125	8	100	7	100	7
Other bilaterals	172	8	147	7	108	4	108	7	137	9	137	10
Debt relief	—	—	—	—	—	—	—	—	—	—	—	—
Paris Club	—	—	—	—	—	—	—	—	—	—	—	—
Syndicated loan	—	—	—	—	—	—	—	—	—	—	—	—
<b>Total</b>	2 189	100	2 164	100	2 780	100	1 513	100	1 450	100	1 362	100

Table 3.1 (continued)

Balance-of-payments support — 1992																
	Total		Disbursements		Commitments		Albania I		Disbursements		Commitments		Estonia		Disbursements	
	Commitments	%	Disbursements	%	Commitments	%	Disbursements	%	Commitments	%	Disbursements	%	Commitments	%	Disbursements	%
	Million USD		Million USD		Million USD		Million USD		Million USD		Million USD		Million USD		Million USD	
IFIs	1 564	69	1 193	71	48	29	28	23	116	57	109	69				
IMF	909	40	768	46	28	17	18	15	86	42	83	53				
World Bank (policy-based)	655	29	426	26	20	12	10	8	30	15	26	17				
<b>Bilaterals</b>	708	31	476	29	115	71	95	77	87	43	48	31				
European Union	423	19	298	18	83	51	83	67	46	22	23	14				
USA	0	0	0	0	0	0	0	0	0	0	0	0				
Japan	120	5	79	5	20	12	9	7	20	10	13	8				
Other bilaterals	165	7	100	6	12	8	4	3	22	11	13	8				
<b>Total</b>	2 272	100	1 670	100	162	100	123	100	204	100	158	100				
	Latvia		Disbursements		Commitments		Lithuania		Disbursements		Commitments		Romania II		Disbursements	
	Commitments	%	Disbursements	%	Commitments	%	Disbursements	%	Commitments	%	Disbursements	%	Commitments	%	Disbursements	%
	Million USD		Million USD		Million USD		Million USD		Million USD		Million USD		Million USD		Million USD	
IFIs	215	56	196	68	245	53	194	62	940	89	666	85				
IMF	170	44	151	52	185	40	149	48	440	42	366	47				
World Bank (policy-based)	45	12	45	16	60	13	45	14	500	47	300	38				
<b>Bilaterals</b>	169	44	94	32	217	47	120	38	119	11	119	15				
European Union	91	24	46	16	114	25	57	18	90	8	90	11				
USA	0	0	0	0	0	0	0	0	—	0	—	0				
Japan	35	9	23	8	45	10	34	11	—	0	—	0				
Other bilaterals	43	11	25	9	58	13	29	9	29	3	29	4				
<b>Total</b>	384	100	290	100	462	100	314	100	1 059	100	785	100				

Table 3.1 (continued)

Balance-of-payments support — 1994												
	Total				Albania II				Algeria II			
	Commitments		Disbursements		Commitments		Disbursements		Commitments		Disbursements	
	Million USD	%	Million USD	%	Million USD	%	Million USD	%	Million USD	%	Million USD	%
IFIs	4 086	27	2 772	21	75	63	42	70	1 397	19	1 182	17
IMF	3 206	21	2 072	16	60	50	34	58	1 097	15	882	13
World Bank (policy-based)	880	6	700	5	15	13	8	13	300	4	300	4
<b>Bilaterals</b>	11 299	73	10 357	79	45	37	18	30	5 920	81	5 666	83
European Union	952	6	336	3	41	34	18	30	335	5	201	3
USA	100	1	90	1	0	0	0	0	0	0	0	0
Japan	350	2	185	1	0	0	0	0	150	2	95	1
Other bilaterals	252	2	101	1	4	3	0	0	135	2	70	1
Debt relief	9 645	63	9 645	73	—	—	—	—	5 300	72	5 300	77
London Club	4 920	32	4 920	37	—	—	—	—	1 120	15	1 120	16
Paris Club	4 380	28	4 380	33	—	—	—	—	4 180	57	4 180	61
Other	345	2	—	—	—	—	—	—	—	—	—	—
<b>Total</b>	15 385	100	13 129	100	120	100	59	100	7 317	100	6 848	100
	Commitments		Bulgaria II		Commitments		Moldova I		Commitments		Romania III	
	Million USD	%	Disbursements	%	Million USD	%	Disbursements	%	Million USD	%	Disbursements	%
			Million USD				Million USD				Million USD	
IFIs	646	13	195	5	164	56	133	56	913	81	447	100
IMF	521	11	195	5	104	35	121	51	713	63	247	55
World Bank (policy-based)	125	3		0	60	20	12	5	200	18	200	45
<b>Bilaterals</b>	4 214	87	4 088	95	130	44	106	44	218	19	0	0
European Union	125	3	88	2	54	18	30	12	143	13	0	0
USA	0	0	0	0	30	10	20	8	0	0	0	0
Japan	50	1	0	0	40	14	30	13	50	4	0	0
Other bilaterals	39	1	0	0	6	2	26	11	26	2	0	0
Debt relief	4 000	82	4 000	93	—	—	—	—	—	—	—	—
London Club	3 800	78	3 800	89	—	—	—	—	—	—	—	—
Paris Club	200	4	200	5	—	—	—	—	—	—	—	—
Other	—	—	—	—	—	—	—	—	—	—	—	—
<b>Total</b>	4 860	100	4 283	100	294	100	239	100	1 131	100	447	100
	Commitments		Slovakia		Commitments		Ukraine					
	Million USD	%	Disbursements	%	Million USD	%	Disbursements	%				
			Million USD				Million USD					
IFIs	426	64	308	84	465	47	465	53				
IMF	346	52	228	62	365	37	365	41				
World Bank (policy-based)	80	12	80	22	100	10	100	11				
<b>Bilaterals</b>	242	36	60	16	530	53	420	47				
European Union	155	23	0	0	100	10	0	0				
USA	0	0	0	0	70	7	70	8				
Japan	60	9	60	16	0	0	0	0				
Other bilaterals	27	4	0	0	15	2	5	1				
Debt relief	—	—	—	—	345	35	345	39				
London Club	—	—	—	—	—	—	—	—				
Paris Club	—	—	—	—	—	—	—	—				
Other	—	—	—	—	345	35	345	39				
<b>Total</b>	668	100	368	100	995	100	885	100				

**Table 4****Selected economic indicators**

	1992	1993	1994	
			Programme <sup>1</sup>	Estimates
GDP at constant prices (percentage change)				
Albania	- 9,7	11,0	8,0	7,4
Algeria	2,2	- 1,8	3,0	0,1
Bulgaria	- 7,3	- 2,4	0,0	1,4
Estonia	- 19,3	- 3,5	6,0	6,0
Latvia	- 35,0	- 15,0	—	2,0
Lithuania	- 37,7	- 16,2	—	2,0
Moldova	- 29,1	- 8,7	- 3,0	- 22,2
Romania	- 13,6	1,3	—	3,4
Slovakia	- 7,0	- 4,1	0,0	4,8
Ukraine	- 17,0	- 17,1	- 23,0	- 23,0
Consumer price (end-year) (percentage change)				
Albania	236,6	30,9	24,0	15,8
Algeria	31,7	20,5	38,7	29,2
Bulgaria	79,4	63,8	30,0	121,9
Estonia	942,0	36,0	—	42,0
Latvia	958,0	35,0	—	26,0
Lithuania	246,0	163,0	—	45,0
Moldova	2 198,0	837,0	123,0	116,0
Romania	198,5	295,0	77,0	61,7
Slovakia	9,1	25,1	12,0	11,7
Ukraine	2 000,0	10 155,0	276,0	401,0
Fiscal balance (percentage of GDP)				
Albania	- 21,8	- 16,0	- 16,5	- 14,0
Algeria	- 1,3	- 9,2	- 5,7	- 5,0
Bulgaria	- 15,0	- 15,7	- 6,2	- 6,7
Estonia	0,2	0,7	—	0,0
Latvia	- 0,8	0,6	—	- 4,1
Lithuania	0,5	- 5,1	—	- 4,0
Moldova	- 23,4	- 6,8	- 3,7	- 8,1
Romania	- 4,6	- 0,1	- 2,5	- 2,3
Slovakia	- 13,1	- 7,6	- 4,0	- 2,7
Ukraine	- 30,4	- 10,1	- 9,4	- 8,6

**Table 4 (continued)****Selected economic indicators**

	1992	1993	1994	
			Programme <sup>1</sup>	Estimates
Current account (percentage of GDP)				
Albania	- 65,7	- 33,4	- 17,3	- 13,5
Algeria	2,9	2,1	- 6,3	- 4,2
Bulgaria	- 9,3	- 7,9	- 5,9	1,0
Estonia	7,6	0,7	- 9,2	- 6,4
Latvia	2,3	6,7	—	- 3,4
Lithuania	3,4	- 6,2	—	- 5,1
Moldova	- 3,0	- 9,3	- 12,5	- 9,2
Romania	- 8,6	- 5,5	- 3,5	- 1,0
Slovakia	0,0 <sup>2</sup>	- 5,4	- 2,6	6,0
Ukraine	- 3,5	- 5,9	- 6,8	- 6,0
Official foreign exchange reserves (end-year)				
(months of imports)				
Albania	0,7	2,2	3,1	3,3
Algeria	2,2	2,3	1,8	2,9
Bulgaria	3,5	2,4	2,7	3,5
Estonia	4,5	4,8	—	4,3
Latvia	2,0	4,4	—	4,6
Lithuania	2,6	2,4	—	2,3
Moldova	0,0	1,5	1,0	3,1
Romania	0,2	0,1	1,1	1,1
Slovakia	0,5	0,6	1,3	2,4
Ukraine	—	0,2	—	0,6

<sup>1</sup> Programme targets as set in July 1993 (and revised in August 1994) for Albania, May 1994 for Algeria, April 1994 for Bulgaria, December 1993 (and revised in May 1994) for Moldova, May 1994 for Romania, July 1994 for Slovakia, October 1994 for Ukraine.

<sup>2</sup> After fiscal transfers from the Czech lands, estimated at about 7% of Slovak GDP.

Source: National authorities.

**Table 5****Status of economic reform**

<b>5.1. Albania</b>	
1. Price liberalization	Most price controls and subsidies eliminated, with the exception of energy. Energy prices adjusted in order to reach progressively the cost-covering level.
2. Trade liberalization	No quantitative restrictions on imports. Export restrictions limited to scrap metals.
3. Exchange regime	Free float since July 1992 within a unified exchange market. Early licensing of foreign exchange dealers and exchange bureaux. Current-account convertibility. Agreement in principle on the large external debt arrears to commercial banks reached in May 1995.
4. Foreign direct investment	Liberal legislation. Draft law on liberalization of land sale recently presented to the Parliament.
5. Monetary policy	Use of bank-by-bank credit ceilings. Interest rates are set administratively to ensure that they remain positive in real terms. Treasury bill auctions (3, 6, 12 months).
6. Public finances	VAT introduction approved in late 1995. Removal of tariff exemptions, new classification, new tariff rates approved in May 1995. Revenue: 28% of GDP in 1994. Expenditure shifting away from subsidies and social benefits towards public investment.
7. Privatization and enterprise restructuring	In all, 96% of total arable land privatized. Distribution of titles completed in May 1995. Draft laws to facilitate the emergence of a land market (May 1995). Small-scale privatization in trade and services completed. Industrial enterprises: privatization of small and medium-sized enterprises largely completed; mixed progress with biggest State-owned enterprises. Draft laws on a mass privatization scheme (March 1995).
8. Financial sector reform	Two-tier banking system. Three existing State-owned banks still to be restructured, and their non-performing loans replaced by government bonds. Audits due to start in 1995. Streamlining of licensing procedures envisaged to facilitate the entry of new private banks. Important informal banking system.



**Table 5** (*continued*)

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<b>5.2. Algeria</b>	
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1. Price liberalization	Price liberalization is proceeding gradually, with passage of goods from strict price controls to controls on profit margins only and finally to completely free prices. Public utilities and basic staple foods remain under control, but with subsidies being progressively phased out.
2. Trade liberalization	Imports have been fully liberalized, apart from goods subject to health, religious and security checks. A registration scheme for importers, based on professional criteria, will be abolished in the course of 1995. Legal and <i>de facto</i> State import monopolies are rapidly being eliminated.
3. Exchange regime	Following a 40% devaluation of the dinar in April 1994, the foreign exchange allocation system has been substantially liberalized and foreign exchange is now available for all bona fide imports by enterprises. Switch from fixed to managed float exchange rate but continuing large difference between official and parallel markets rates. Convertibility of the dinar for current-account transactions is expected to be reached in the course of 1996.
4. Foreign direct investment	A liberal foreign investment regime, including the banking sector, was adopted in 1993. However, no significant foreign investments have taken place in view of the security situation.
5. Monetary policy	Interest rates have increased in 1994 but remain negative in real terms. A cap on the margin between debtor and creditor rates limits profitability and competition in the banking sector.
6. Public finances	The public sector deficit has been reined in from 9,2% of GDP in 1993 to 5% in 1994, mainly through strict wage controls and reductions in subsidies.
7. Privatization and enterprise restructuring	Most State-owned enterprises have received autonomous status and are now controlled by several State participation funds. The remaining 23 non-autonomous enterprises will undergo financial restructuring before becoming autonomous by end-1995. A pilot hotel privatization programme has been launched and a privatization law is in preparation.
8. Financial sector reform	Banks are State-owned and have developed very little private sector credit activities. Short of privatization, management contracts are proposed for 1995. Prudential regulations and banking supervision are being set up in the wake of extensive banking audits.

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**Table 5** (*continued*)

<b>5.3. Bulgaria</b>	
1. Price liberalization	At present some 90% of all retail turnover takes place under a free price regime. Price controls still maintained on some public services (energy, telecommunications, water supply and transport). In these sectors, prices remain below cost. In April 1994, a new temporary price 'monitoring' was introduced on some basic food items.
2. Trade liberalization	Export prohibitions have been removed (temporary exception: grain, until September 1994). Average import tariff on industrial goods: 22%. Some import protection measures are still in place. Interim and trade agreements with the European Union and EFTA entered into force on 1 January 1994.
3. Exchange regime	Since 1991, unified and quasi-free floating exchange-rate regime. Internal current-account convertibility established (few restrictions). Limited Bulgarian National Bank (BNB) interventions in support of the lev. Official (Paris Club) debt rescheduling reached in April 1994. This was followed by the finalization of DDSR arrangement with (London Club) commercial creditors in July.
4. Foreign direct investment	Liberal foreign investment legislation adopted in early 1992. Small amounts of foreign investment recorded so far due to external debt problems, policy slippages and political uncertainty.
5. Monetary policy	Bank credit ceilings were discontinued in mid-1994. In 1994, monetary and credit indicators used as nominal anchor. Limited open market operations in 1994.
6. Public finances	New rules on tax administration adopted in 1994. VAT entered into force in April of same year. Revenue/GDP ratio in 1994: 38,1% — budget deficit/GDP ratio: 6,7.
7. Privatization and enterprise restructuring	Property restitution programme well advanced. A financial rescue plan for enterprises was initiated in 1994. Mass privatization programme (involving 500 enterprises) postponed. Standard market-based privatization proceeded only slowly.
8. Financial sector reform	In 1994, banking supervision strengthened. Bank consolidation programme carried out by Bank Consolidation Company almost completed. Clean-up operations and bank recapitalization proceeded slowly in 1994. Stock exchange introduced and developing slowly.

**Table 5** (*continued*)

<b>5.4. Estonia</b>	
1. Price liberalization	Major price liberalization in 1991. Since end-1992, virtual completion of price liberalization, including in the energy sector.
2. Trade liberalization	In early 1992, abolition of most import tariffs (except for a few luxury goods), and of most remaining quotas and licensing requirements, except for oil, shale, clay and quartz. Imports subject to a 0,5% administrative fee plus 18% VAT. Few export tariffs. Free trade agreement with Baltic and Nordic countries. Free trade agreement with the European Union.
3. Exchange regime	Current-account convertibility. Since 1992, Estonian kroon pegged to the Deutschmark, at a rate of eight kroons to one Deutschmark, under a currency board system.
4. Foreign direct investment	Free repatriation of profits and proceeds of liquidation of investment by non-residents.
5. Monetary policy	Central bank responsible for operation of currency board (Issue Department) and, in exceptional cases, for emergency lending to banking system (Banking Department, responsible for managing reserves in excess of currency board cover). Central bank does not interfere with the commercial banks' setting of interest rates.
6. Public finances	General government revenue: 35% of GDP. Personal income tax and VAT introduced in 1991, and turnover tax replaced by corporate income tax; social security, natural resource and specific excise taxes.
7. Privatization and enterprise restructuring	Bankruptcy Law enacted in 1992. Almost completed small-scale privatization (about 1 500 SMEs privatized). Enactment of the Privatization Law and establishment of the Estonian Privatization Office in 1993 to accelerate the privatization process. Wide distribution of vouchers; large-scale privatization accelerated in 1994 (258 enterprises privatized by year-end).
8. Financial sector reform	Two-tier banking system. Increased pressure on State enterprises to restructure through hard budget constraints and selective application of the Bankruptcy Law. Reduction of number of commercial banks from 40 to 24 through increase in minimum capital requirement following a banking crisis in winter 1992-93. Stock exchange introduced. Recent enactment of Credit Institutions Act enhanced supervision and prudential regulation powers of the central bank.

**Table 5** (*continued*)

<b>5.5. Latvia</b>	
1. Price liberalization	Since end-1992, price liberalization essentially completed, excluding utility prices and rents.
2. Trade liberalization	All export quotas, licensing and most export tariffs abolished in 1992. No licensing requirements for imports, but various import tariffs. Free trade agreement with Baltic and Nordic countries. Free trade agreement with the European Union.
3. Exchange regime	Current-account convertibility. Exchange rate unified. Exchange rate of the lats stabilized under managed floating system, informally pegged to the special drawing right (SDR).
4. Foreign direct investment	Free repatriation of profits and proceeds of liquidation of investment by non-residents.
5. Monetary policy	Independent central bank. Strict monetary policy resulted in lowest inflation rate among Baltic States. Credit policy through indirect instruments.
6. Public finances	General government revenue: 36% of GDP. New tax system since January 1991. VAT introduced in February 1992. In 1993, replacement of progressive income tax by flat-rate tax (25%) plus a 10% surcharge on annual income. Sale of treasury bills to finance general government budget deficit.
7. Privatization and enterprise restructuring	Substantial progress on small-scale privatization. Privatization agency established in 1994. Large-scale privatization delayed, pending settlement of property rights issues, until auctions of 68 large enterprises launched in November 1994. Large distribution of vouchers, including for land and housing privatization. State enterprises not ready for immediate privatization transformed into stock companies, to be managed by a State property fund established in 1994. Slow progress on liquidation.
8. Financial sector reform	Two-tier banking system. Former branches of the Bank of Latvia either merged, now forming the Universal Bank, or privatized, except for one which was liquidated. Capital adequacy ratio increased in January 1994. Balance sheets of Universal Bank of Latvia and of Latvian Savings Bank recently strengthened. However, financial system fragile. Nine bank licences withdrawn in 1994. Crisis of Baltija Bank, the main commercial bank in Latvia. Stock exchange already introduced.

**Table 5** (*continued*)

<b>5.6. Lithuania</b>	
1. Price liberalization	Price liberalization in 1991, 1992 and 1993. Level of subsidization reduced for household heating (prices raised by 50% in October 1994), electricity (prices raised by 33% in October 1994), and transport.
2. Trade liberalization	Export quotas and licensing completely removed in June 1993. All import controls and licences removed. Since May 1994, import tariffs for a wide range of goods, representing two thirds of imports, suppressed. In 1994, import tariffs on several agricultural goods raised to average 30% in October. Free trade agreement with the European Union entered into force on 1 January 1995. Free trade agreement with Baltic and Nordic countries.
3. Exchange regime	Current-account convertibility. Since April 1994, litas pegged to US dollar at a fixed rate of four litas to one US dollar.
4. Foreign direct investment	Free repatriation of profits and proceeds of liquidation of investment by non-residents.
5. Monetary policy	New Central Bank Law enacted in December 1994. Since April 1994, currency board arrangement, according to which the money in circulation is limited to the amount of foreign exchange held in the central bank.
6. Public finances	General government revenue: 24% of GDP. The tax system was reformed and now includes personal income and profit taxes, property tax, natural resource tax, individual excise taxes, as well as general sales tax. New value-added tax replacing previous general excise tax.
7. Privatization and enterprise restructuring	Bankruptcy Law enacted in 1992. Substantial progress on small and large-scale privatization through auctions, public shares subscriptions and voucher system. By January 1994, 76% of all companies eligible for privatization (one third of State capital) privatized. Little progress on land privatization.
8. Financial sector reform	Two-tier banking system since 1992. State Commercial Bank taking over commercial functions of Bank of Lithuania. Commercial Banking Act enacted in early 1995. Three main State-owned banks currently audited. Stock exchange already introduced.

**Table 5** (*continued*)

<b>5.7. Moldova</b>	
1. Price liberalization	Liberalization of prices, goods and services with some exceptions (mainly energy products and cereals).
2. Trade liberalization	All export quotas removed with the exception of grain and grain products. Maximum import tariff lowered to 50% by end-1994, to 30% by end of March 1995, and to be lowered to 20% by end of November 1995.
3. Exchange regime	New currency introduced in November 1993. Freely floating. Daily interbank foreign exchange auctions. Current-account convertibility.
4. Foreign direct investment	Liberal regime: free repatriation of profits and proceeds of liquidation of investments within the three months of the closure.
5. Monetary policy	Relying on credit ceilings. Key objective: rapid and sustained reduction of inflation, based on introduction of new currency, enforced financial discipline and enhanced central bank independence. New draft Banking Law to be adopted shortly by Parliament, providing independence of the national bank in conducting monetary policy.
6. Public finances	VAT since 1993. Tax collection impeded by important barter trade, predominance of cash transactions and liquidity problems in enterprise sector. Assumption by the government of guaranteed loans to enterprises in default to be strictly limited in 1995. Revenue/GDP ratio: 16,9%.
7. Privatization and enterprise restructuring	Delay in the 1993-94 privatization programme, but important acceleration during the last months of 1994 (25% of State assets privatized by end-1994). New programme for 1995-96 adopted in March 1995, by which two thirds of State assets should be privatized by end-1996. Diversification of privatization process in the new programme, compared with 1993-94 programme only based on vouchers (patrimonial bonds). Under present Bankruptcy Law, more than 90 private enterprises already liquidated and bankruptcy proceedings initiated against seven State enterprises.
8. Financial sector reform	Two-tier banking system. National bank working on new regulations to meet standards set up by the Basle Committee. New regulation imposing provisions for bad loans recently approved.



**Table 5** (*continued*)

<b>5.8. Romania</b>	
1. Price liberalization	Completed in May 1993. Energy prices remain controlled but adjusted regularly for changes in international prices. Public utilities and some basic staple food prices still controlled and subsidized.
2. Trade liberalization	Fully liberalized. A limited number of import/export quota/bans are still in force, either for health reasons or for subsidized goods. Europe Agreement with the European Union in force since 1 February 1995. Most-favoured-nation (MFN) status in the USA.
3. Exchange regime	Limited current-account convertibility. A market-based exchange-rate regime was established in April 1994 but multiple exchange rates persist. Foreign exchange available to individuals through private exchange bureaux.
4. Foreign direct investment	Free legal environment for equity participation and profits repatriation by non-residents. Lack of progress with respect to privatization has limited the volume of investment inflows.
5. Monetary policy	The central bank uses both direct and indirect instruments for monetary policy management. Positive real interest rates have strengthened confidence in the leu. Central bank financing of Treasury deficits has almost ceased. Weak financial discipline of State companies.
6. Public finances	Good progress with fiscal reforms and introduction of new taxation systems, including VAT. Overhaul of the income tax system is expected by end-1996. Fiscal deficit is relatively low and under control.
7. Privatization and enterprise restructuring	Little progress with medium-sized and large enterprise privatization through the State Ownership Fund. Some success with small-scale privatization through buy-outs. Large inter-enterprise arrears hamper financial restructuring of loss-makers. Private sector amounts to about a third of GDP.
8. Financial sector reform	Two-tier banking system. Several foreign banks already operational. Clearing of interbank payments and transfers remains very slow. Very little progress with privatization of former State-owned banks.

**Table 5** (*continued*)

<b>5.9. Slovakia</b>	
1. Price liberalization	In all, 96% of total turnover based on free prices, with regulation still in force in the areas of energy, public transportation, rents, telephone, telegraph, and pharmaceutical products.
2. Trade liberalization	Imports liberalized except for a few sensitive items subject to import licences. Export licensing remains for a limited number of products. Free trade agreements with the European Union, the EFTA countries and the Visegrad countries. Customs union with Czech Republic since dissolution of the Czech and Slovak Federal Republic (CSFR). A 10% temporary surcharge on consumer imports was introduced in March 1994.
3. Exchange regime	Current-account convertibility almost completed in early 1991. Exchange rate pegged to a basket of Western currencies since February 1993. Transactions with Czech Republic conducted through a clearing system at a different exchange rate. The authorities plan to reach full current-account convertibility by 1 January 1996. This will involve termination of clearing system with Czech Republic.
4. Foreign direct investment	No limits on equity participation in enterprises by non-residents, except in the case of a few sensitive or defence-related sectors. Free repatriation of profits and proceeds from the liquidation of investment.
5. Monetary policy	National Bank of Slovakia, established in January 1993, operates independently of government. Slovak crown introduced in February 1993. Individual credit ceilings on banks reintroduced in March 1994.
6. Public finances	VAT reformed, excise tax system and personal income tax introduced in January 1993. General government revenues estimated at 50,6% of GDP in 1994.
7. Privatization and enterprise restructuring	First wave of large-scale privatization completed by spring 1993. Second wave, under preparation, will emphasize traditional privatization methods (direct sales, tenders, etc.). Second scheme of voucher privatization to be completed by mid-1996. A Bankruptcy Law came into effect in June 1993 but few companies have filed for bankruptcy.
8. Financial sector reform	Two-tier banking system established in January 1990. Major financial institutions privatized under first wave of large-scale privatization. However, State Savings Bank and biggest commercial bank (VUB) remain State-controlled. Since 1991, several measures to strengthen banks' balance sheets. Bratislava Stock Exchange in operation since 1993 but financial markets remain underdeveloped. Stricter rules for classification and provisioning of bad loans introduced in March 1995.

**Table 5** (*continued*)

<b>5.10. Ukraine</b>	
1. Price liberalization	Limits on profit margins abolished. Price regulation limited to natural and a small number of artificial monopolies. Full cost of imported energy passed on to industrial and agricultural users. Sharp increases in coal, electricity, gas, transportation and housing prices for households.
2. Trade liberalization	<p>System of State orders abolished. Budget allocations for 1995 for State procurement of agricultural products limited to needs of budgetary organizations. At least half of these priced by tender or through commodity exchanges.</p> <p>Import regime free of quantitative restrictions, with few exceptions, primarily for health and safety reasons. Maximum import tariff lowered to 30%. Elimination of all export quotas and licences, except for quotas on grain. Auction mechanism for allocating externally imposed quotas initiated.</p>
3. Foreign exchange regime	Abolition of official exchange rate and unification of exchange rate determined at interbank auction market. High degree of current-account convertibility reinstated. Managed floating of the exchange rate of the karbovanets.
4. Foreign direct investment	Decree of May 1993 grants tax relief (exemption from income and profit tax for five years) for certain investments constituting at least 20% of an enterprise's charter capital.
5. Monetary policy	Allocation of all central bank credit to commercial banks by auction. No more directed credits issued. Central bank refinance rate adjusted to ensure that it remains positive in real terms.
6. Public finances	Since 1992, gradual tightening and rationalization of budget, including reform of VAT, enterprise and income taxes. Reduction of public expenditure from 72%, as percentage of GDP, in 1992 to some 50% in 1994. Revenue/GDP ratio: 44,3% in 1994.
7. Privatization and enterprise restructuring	Mass voucher privatization programme launched at beginning of 1995. Approximately 400 medium-sized and large enterprises privatized. Progress with small-scale privatization. Decision to close some 15 loss-making coalmines. Bankruptcy procedures being simplified in 1995.
8. Financial sector reform	Central Bank Law submitted to Parliament. Plans to strengthen supervision and regulation of the banking sector. Study in preparation on restructuring of portfolio of non-performing loans of largest banks, and auditing in process. Profit tax for banks reduced to 40%.

## II — Albania

### 1. Introduction

Albania's macroeconomic and structural adjustment efforts were initiated in 1992 against a background of severe economic, social and administrative dislocation. The government's decisive efforts to address the crisis when it assumed office in April 1992 have been largely successful. The economic programme for the period mid-1992 to mid-1993, which was supported by an IMF stand-by arrangement and complementary financial assistance from the European Community<sup>1</sup> (ECU 72 million in the form of a grant) and bilateral G24 members, reversed the slide into hyperinflation and the downward spiral of output, and initiated profound changes towards a market economy. Against this background, the Albanian authorities could shift from a mostly short-term horizon towards a consistent medium-term approach when they embarked on a three-year comprehensive arrangement with the IMF under an enhanced structural adjustment facility (ESAF) in mid-1993 (USD 60 million). In support of this IMF programme, the Council of Ministers decided on 28 November 1994<sup>2</sup> to grant Albania further macro-financial assistance of up to ECU 35 million in the form of straight grants in the context of an initiative of the G24 aiming at mobilizing a total of USD 72 million.

Albania has been successfully implementing the economic adjustment efforts contemplated in the first and second annual arrangements under the ESAF. A number of structural reforms fell behind schedule during 1994. The Albanian Government, however, has recently taken new initiatives to accelerate structural adjustment.

### 2. Macroeconomic performance

Macroeconomic performance during 1994 was very satisfactory. Inflation in the 12 months to December was reduced to some 15%, compared with a programme target of 24%. Output is estimated to have continued to grow at a sustained pace (some 7.5%, following 11% in 1993), led by private activity in the agriculture, construction and services sectors. The external current account performed better than programmed, owing, in particular, to export buoyancy and sustained private transfers. This successful macroeconomic outturn reflected the maintenance of tight fiscal and monetary policies; in particular, the targeted domestic financing of the budget deficit was contained at 8% of GDP. External reserves remained above programmed levels.

Based on this performance, the Albanian Government and the IMF have recently agreed on a macroeconomic framework and

the main features of the budget for 1995: the objectives include real GDP growth of 6%, a reduction in inflation to 10% (December to December) and a further increase in external reserves. To this end, a key policy instrument is the reduction in the government domestic financing requirement to no more than 7% of GDP.

To achieve this budget objective, the government has decided to implement a new fiscal package that includes the elimination of customs tariff exemptions at the end of January. Furthermore, the authorities agreed to introduce the VAT in mid-1995 to replace the existing turnover tax, to introduce a simplified customs tariff rate system, and to further reduce civil service employment.

These policies are expected to improve further external accounts, allowing for some additional build-up of reserves (before debt rescheduling). Furthermore, with regard to the status of negotiations with external creditors, the authorities have recently reached an agreement on external arrears (of some USD 500 million, excluding interest) with the banks' advisory committee.

Exports still cover only a fraction of import needs. However, reflecting the exodus of young unskilled labour to neighbouring countries (mostly Greece), expatriate remittances account for a significant fraction of national income and largely outweigh exports as a source of foreign exchange (USD 230 to 260 million a year against USD 110 to 140 million in 1993-94). In the circumstances, they have helped to maintain a stable exchange rate and finance the incipient private sector (mostly trade and construction), including through the development of an informal financial sector. The current-account deficit declined sharply (from 66% of GDP in 1992 to 13.5% in 1994), but Albania still relies heavily on public external financing, in particular to meet the investment needs of its infrastructure projects.

### 3. Structural reforms

The early liberalization of prices, foreign trade and the exchange-rate regime have been major achievements of the Albanian Government in recent years. Most price controls and subsidies were eliminated during 1992-93. As regards bread and energy, the government decided to cushion the social impact of these measures through the introduction of a targeted compensation scheme, to be phased out within a limited period. With regard to energy, the price adjustment resulted in a drop of bill collection together with a sizeable increase in 'non-technical losses' (thefts), dramatic power cuts at the end of 1994, and the need to resort to power imports.

<sup>1</sup> Council Decision 92/482/EEC of 28 September 1992.

<sup>2</sup> Council Decision 94/773/EC of 28 November 1994.

Foreign trade has been largely liberalized: there are no quantitative restrictions on imports; on the export side, licensing is only required for a very limited number of goods. The exchange rate has been floating since July 1992 within a unified exchange market, the efficiency and depth of which have been greatly improved by the early licensing of foreign exchange dealers and exchange bureaux (with PHARE technical assistance to the central bank).

Dramatic changes have taken place in the agriculture sector following the privatization of former cooperatives' land and the liquidation of former State farms. Approximately 96% of total arable land is now reported to be in private hands and agricultural output has recovered (increasing by 14 and 7% in 1993 and 1994, respectively). However, land registration is far from complete and since mid-1994, the distribution of temporary property titles has come to a halt; furthermore, the recipients of former State farm land have only the status of 'users' of that land, and the small size of private plots (1,5 ha on average) is an obstacle to further productivity gains, while the consolidation of these strips into larger units is prevented by the lack of an effective land market.

The privatization of small shops and of the public housing sector was implemented quickly in 1992, through direct sales to employees and tenants at token prices. Following the passage of legislation on restitution and compensation in early 1993, the authorities proceeded with the privatization of small and medium-sized enterprises, through a decentralized procedure, under the responsibility of local authorities. At present, the process is largely completed and has allowed these small-scale enterprises to remain in operation and to stimulate private activities. As regards the biggest State-owned enterprises (SOEs), progress so far has been mixed: with an obsolete capital stock, large sections of industry are no longer viable and cannot operate on commercial terms now that budgetary support has been severely reduced. Furthermore, the administration does not have the capacity to carry out a large-scale restructuring, and there is no tradition and experience of export-oriented production and marketing.

Banking sector reform made little progress in 1994. The three specialized State-owned banks (the Savings Bank for household deposits, the National Commercial Bank (NCB) for the enterprise sector, and the Rural Commercial Bank (RCB) for the agriculture sector) are still burdened with bad loans despite previous attempts at cleaning up these debts. In fact, both the NCB and RCB are virtually bankrupt, while the Savings Bank is not fully autonomous from the central bank. In the circumstances, a strategy has not yet been designed for each of these banks. Meanwhile, informal banking activity has developed. This informal sector seems to have been effective and helpful, even though its interest rates are reported to be very high.

In early 1995, the Government of Albania took a series of measures and made new commitments to remedy the situation in different areas.

As regards the agriculture sector, the government has taken the measures needed to establish an effective land market, including completing the land registration and the distribution of 'tapis' (temporary titles), as well as the conversion of 'user' status into that of lessee.

In the area of privatization and enterprise sector reform, specific measures are contemplated in the three categories of large enterprises (the most problematic sensitive enterprises, public utilities and resource-based enterprises, and other enterprises):

- (i) The first category is made up of 32 SOEs under the responsibility of the Enterprise Restructuring Agency (ERA). The government has set clear objectives in terms of privatization or liquidation (the latter requires new legislation); it has also singled out a group of five enterprises which account for about a half of the total number of employees in ERA enterprises, for which an explicit strategy is soon to be adopted.
- (ii) Regarding public utilities and resource-based enterprises, where very little was done in 1994, the government has recently prepared draft legislation in order to allow eventual privatization of those enterprises.
- (iii) The government's objective for the 'other enterprises' is to have them privatized rapidly through a mass privatization scheme. However, special attention will be devoted to the necessity not to hamper strategic foreign investment in the process.

No strategy has yet emerged for the future of the three State-owned banks. Business plans are being prepared, but their scope is essentially limited to the rationalization of the management of the banks. More substance is expected from the results of the external audits that are due to start soon. Then it would be possible to adopt a strategy for these banks. In addition, licensing procedures are to be streamlined in order to facilitate the entry of new banks, and possibly the registration of part of the current informal banking sector.

Meanwhile, the central bank is striving to improve its capacity and effectiveness, in particular through the establishment of instruments of monetary policy that would allow it to go beyond reliance on bank-by-bank credit ceilings.

#### **4. Implementation of macro-financial assistance**

As mentioned above, on 28 November 1994, the Council of Ministers adopted further macro-financial assistance to Albania up to a maximum amount of ECU 35 million. This grant is complementary to assistance provided by the IMF under the three-year ESAF initiated in mid-1993, with a view to ensuring a sustainable balance-of-payments situation and strengthening the reserve position of the country.

The first tranche (ECU 15 million) of this assistance was disbursed in May, following signature of the Memorandum of

Understanding (MOU) laying down the macroeconomic and structural conditionality attached to the assistance.

The disbursement of the second tranche is expected to take place later this year, subject to satisfactory progress being recorded in Albania's application of the ESAF and to a positive evaluation of progress made with respect to structural reforms. In this evaluation, particular attention will be paid to progress in the fields of liberalization, external debt, budgetary reform, public investment, enterprise and banking sectors, and agriculture.





### III — Algeria

#### 1. Introduction

In September 1991, the Council decided to grant an ECU 400 million loan to Algeria, to be disbursed in two tranches.<sup>1</sup> The loan agreement and the corresponding Memorandum of Understanding specifying the conditions for disbursement were signed in December 1991. The first tranche of ECU 250 million was immediately released as the two conditions attached to it — conclusion of a stand-by agreement with the IMF and a commercial debt refinancing and reprofiling agreement between Algeria and its commercial bank creditors — were met.

In accordance with the Memorandum of Understanding, the release of the second tranche of ECU 150 million was subject to two sets of conditions: (i) respect of the quantitative macroeconomic performance criteria agreed in the context of the IMF programme, and (ii) a positive assessment by the Commission of the progress accomplished in specific areas of structural reform. However, by mid-1992, the programme with the IMF had gone off-track and the macroeconomic performance criteria were not complied with.

A new government came to power that halted most of the economic reform programmes and reversed some of the liberalization measures taken. Throughout 1993, strict price controls, administrative imports management and a stringent foreign currency allocations regime choked economic activity. The appreciation of the real exchange rate and lax fiscal policy increased the fiscal deficit. Towards the end of the year, the decline in hydrocarbon exports revenue led to unsustainable pressure on Algeria's debt service capacity.

In this context, negotiations started with the IMF at the end of 1993, which resulted in the approval of a 12-month stand-by arrangement<sup>2</sup> for an amount of approximately USD 1 billion in May. In June, Algeria, for the first time, obtained an agreement from the Paris Club on a rescheduling of bilateral debt service due during the programme period with the IMF. Furthermore, the programme received financial support from the World Bank, the Arab Monetary Fund, the African Development Bank and Japan. The authorities also addressed a request to the Commission for the rapid release of the remaining second tranche of the 1991 assistance package as well as for further macro-financial assistance under the new programme.

#### 2. Macroeconomic performance

Since the adoption of the new economic programme, progress has been made in the stabilization of the economy and the implementation of economic reforms. The Algerian dinar was devalued by some 45% and the fixed exchange-rate regime was replaced by a managed float, aiming at a stabilization of the real effective exchange rate. Prices, imports and access to foreign currency were substantially liberalized. Consumer subsidies have been gradually reduced and a more effective social safety net is being put in place. Financial discipline for State-owned enterprises has been tightened and the first steps towards privatization have been taken.

The fiscal deficit dropped from 9,2% of GDP in 1993 to 5% in 1994 and the 1995 Budget Law is targeted at a 2% deficit. Monetary policy was tightened and interest rates were increased, although not yet at positive levels in real terms. Despite the strong devaluation and a series of price adjustments, inflation increased moderately from 21% in 1993 to 29% in 1994 and monthly inflation is expected not to exceed a 10% annual rate by the end of 1995. Economic growth, however, has not picked up as foreseen under the programme with the IMF. GDP growth for 1994 was revised downwards from 3% to around zero, which was partly attributable to a drought affecting agricultural production and also to political and security problems which may, if the trend is not reversed, hamper the proper implementation of the economic reform programme.

Export revenue, mostly from hydrocarbon products, further declined in 1994, in spite of an increase in world oil prices. Imports increased by 15% following the liberalization of the import and foreign exchange regimes. Shortages of consumer and investment goods have been eliminated. As a result of these liberalizations, the current account deteriorated, as foreseen under the programme, from a USD 0,8 billion surplus in 1993 to a USD 1,7 billion deficit in 1994 and the overall balance of payments registered a USD 4,4 billion deficit in the same year. This has been financed mainly through bilateral debt rescheduling agreed with the Paris Club (the equivalent of some USD 3,6 billion). Negotiations with the London Club of commercial bank creditors were also started but have not as yet come to a final conclusion. Commercial debt service reduction contributed some USD 0,8 billion to balance-of-payments financing in 1994.

Exceptional financing has permitted the Bank of Algeria to clear approximately USD 0,5 billion of arrears and strengthen its international reserve position, which reached nearly USD 2,2 billion (2,4 months of imports) at end-1994, up from USD 1,4 billion early in 1994.

<sup>1</sup> Decision 91/510/EEC of 23 September 1991.

<sup>2</sup> Combined with a compensatory and contingency financing facility.

### 3. Structural reforms

Stringent administrative import controls and foreign currency allocations were abolished in April 1994 and replaced by a more liberal regime comprising a system of professional criteria for importers and a limited list of prohibited imports. The latter list was gradually reduced and was abolished at the end of 1994, except for goods prohibited for religious and security reasons. The list of goods subject to professional criteria is also being reduced and is expected to be abolished towards the end of 1995. State monopolies on certain imports have also been eliminated. Access to foreign currency has been completely liberalized for all visible current-account transactions by private and public enterprises. Only imports financed through foreign credits are still subject to authorization.

Since 1992, the five State-owned banks have been regularly audited and institutional development plans have been put in place. The Bank of Algeria has strengthened its supervisory capacity and established more effective prudential regulations and controls. Although banks are free to set their own creditor and debtor interest rates, a ceiling of 5 percentage points has been imposed on the spread between average creditor and debtor rates for each bank. In 1995, management contracts are expected to be signed between the Ministry of Finance and bank managers. Banks will receive a banking licence provided that prudential ratios, set by the Bank of Algeria, are respected.

The legal environment for private enterprises improved considerably. A commercial code was promulgated in 1993, putting private and public enterprises on an equal legal footing. The investment code authorizes foreign investments in all sectors of the economy and provides for the full repatriation of profits. A Competition Law was adopted in January 1995 which liberalizes the price regime and puts stringent limits on cartels and monopolies.

Nearly 400 public enterprises were given autonomous status in 1992 and their management was transferred to several participation funds. Restructuring plans have been prepared for the remaining 23 non-autonomous public enterprises and, following the signature of management contracts and a one-off injection of rehabilitation funds by the Treasury, they are scheduled to become autonomous by the end of 1995.

The possibility to privatize public enterprises was first introduced in the 1994 Budget Law which authorized the sale of public assets. A pilot privatization programme comprising five hotels was launched in November 1994. A Privatization Law and a more comprehensive privatization programme are currently in preparation. In Algeria, the present political and security situation is, of course, not conducive to private sector domestic and foreign investments.

### 4. Implementation of macro-financial assistance

Following the agreement in principle between the Algerian authorities and the IMF in April 1994 and a request for further macro-financial assistance from the Algerian authorities, the Council endorsed the Commission's intention to release the remaining second tranche of the 1991 programme and agreed in principle on additional macro-financial assistance for an amount of ECU 200 million.

The second tranche of ECU 150 million was effectively disbursed in August and the Commission proposal for an additional ECU 200 million of macro-financial assistance, to be disbursed in two tranches, was adopted by the Council on 22 December 1994.<sup>1</sup> A Memorandum of Understanding specifying the conditions related to the disbursement of the first tranche of ECU 100 million was agreed with the Algerian authorities in early 1995. The structural reform conditions relate to further liberalization of the imports and exchange-rate regimes, reforms in the financial sector and progress towards restructuring and privatization of public enterprises. Furthermore, the Memorandum emphasizes Community concerns in the social sector and synergy between macro-financial assistance and other Community aid instruments, which could facilitate the implementation of economic reforms in Algeria. Disbursement of this first tranche will take place as soon as the economic reforms agreed upon in the Memorandum have been implemented, normally by mid-1995, and provided that the IMF programme remains on-track.

The conditions related to the release of the second tranche will be negotiated at a later stage, after the disbursement of the first tranche and the approval by the IMF board of a new programme with Algeria.

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<sup>1</sup> Decision 94/936/EC of 22 December 1994.

# IV — Baltic countries

## 1. Introduction

The three Baltic States, which recovered their sovereignty in August 1991, had already initiated reforms under the past regime after the adoption by the Supreme Soviet of the bill on their economic independence in November 1989. In 1992, as they were already actively engaged in reforms to a market economy, economic prospects worsened. The dismantling of trade relations among former Soviet republics and the increase in prices of energy imports from Russia to world levels resulted in a trade shock and an expected deficit in their external accounts which were expected to be unsustainable without international support. The three countries defined stabilization and reform programmes covering the period mid-1992 to mid-1993 and concluded stand-by arrangements with the IMF. G24 donors were called to contribute to filling the remaining expected balance-of-payments gap for the programme period, estimated at a level of USD 105 million for Estonia, USD 210 million for Latvia and USD 285 million in the case of Lithuania. On the basis of favourable prospects of support within the G24, the IMF board approved the stand-by arrangements in September and October 1992.

In November 1992, the EC Council approved macro-financial assistance of up to ECU 220 million<sup>1</sup> for the three countries (ECU 40 million for Estonia, ECU 80 million for Latvia and ECU 100 million for Lithuania) in support of the countries' programmes. The bulk of the remaining bilateral support within the G24 came from Japan and the EFTA countries. Loan agreements and Memoranda of Understanding between the Community and each beneficiary were signed in early 1993. The Commission disbursed the first tranches (50% of the loan amounts) in March 1993 for Estonia and Latvia, and in July 1993 for Lithuania. The release of the second tranches was made subject to positive evaluation of performance criteria, regarding both macroeconomic stabilization aspects and progress of structural reforms, as set in the Memoranda of Understanding.

## 2. Recent economic developments

### Estonia

Estonia had already started to implement liberalization measures, mainly on prices, under the previous Soviet regime in 1990 and 1991. The Bank of Estonia was re-established in 1990. In March 1992, most import duties were abolished, except on a few goods like cars, tobacco and alcohol. Price liberalization had been almost completed by mid-1992. In June

1992, the Estonian kroon was introduced and pegged to the Deutschmark at a rate of eight kroons to one Deutschmark under a currency board arrangement. The new restrictive monetary policy, which under the currency board is constrained by the level of foreign exchange reserves held in the central bank, proved successful in stabilizing the economy and bringing inflation back down to two-digit levels in 1993. The kroon parity *vis-à-vis* the Deutschmark has not been modified since 1992.

The latest developments are favourable. The economy emerged from recession by the end of 1993 and GDP is estimated to have grown by 6% in 1994, despite a severe drought which hampered agricultural production. Monetary growth under the currency board discipline remained moderate and fell to a level of 30%. The general government budget was in balance overall, reflecting improvements of revenue performance. However, inflation remained high with the consumer price index (December to December) increasing by 47%. After the establishment of the Estonian Privatization Office in 1993 whose aim was to coordinate better the policies directed towards the enterprise sector, privatization accelerated in early 1994. While the process of small-scale privatization is almost complete with 1 500 small enterprises sold, 258 large-scale enterprises had also been sold by the end of the year.

The shift of the country's trade to the West was sharp: in 1994, EU and EFTA countries accounted for 65% of exports and over 70% of imports. The recovery of growth and of investment-related imports led to substantial imports. Despite a sharp growth of exports, the trade balance last year was negative for the first time since 1991 and the current-account deficit reached 6.5% of GDP. However, owing to substantial inflows of private foreign direct investments, the capital account recorded a substantial surplus, which allowed foreign exchange reserves to continue increasing. On 1 January 1995, the free trade agreement with the European Union entered into force. A Europe Agreement was signed in June 1995. Estonia became an associated country to the European Union.

The programme under the IMF stand-by arrangement for the period October 1993 to March 1995 remained on-track and in March 1995 the Fund approved a new stand-by arrangement of an amount of SDR 14 million (about USD 21 million) for a new 15-month period. However, it is expected that the Estonian authorities will not draw on this facility unless it is needed.

### Latvia

Reforms in Latvia had already started under the previous Soviet regime, as in the other Baltic States. Prices and the external trade liberalization were fully completed by mid-1992. A two-tier banking system was established in 1992. In mid-1992, the

<sup>1</sup> Decision 92/542/EEC (OJ L 351, 2.12.1992, p. 29).

country left the rouble zone, introduced a temporary currency (the Latvian rouble) and initiated stabilization measures, in particular a strict monetary policy, and further structural reforms. Latvia pursued a strict budgetary discipline, which led to a surplus of the general government budget in 1993 (0,6% of GDP) after a low deficit in 1992 (0,8%). The privatization of small firms was initiated in 1992. A national currency, the Lats, was introduced in summer 1993. The tight stabilization measures produced significant results. By the end of 1993, inflation had been brought down to 35% (December to December).

Developments in 1994 were mainly positive. After a sharp contraction of output during the previous years (GDP fell by 35% in 1992 and 15% in 1993), GDP stabilized and started to grow again by 2%. Inflation continued to decline to a 26% level (December to December). The financial deficit of the budget was kept within the 2% target, despite significant wage and pension increases. However, owing to the authorities' decision to lend to the Latvian electricity utility to clear external gas arrears *vis-à-vis* Russia, the fiscal deficit which stood at 4% of GDP was higher than anticipated.

While exports remained stable relative to 1993, imports grew significantly in 1994, which led to a significant current-account deficit of about 3,4% of GDP, against a surplus in 1993. However, as in 1993, the capital account was in surplus mainly due to large private capital inflows, which allowed for a further consolidation of the country's level of foreign exchange reserves, worth five months of imports. On 1 January 1995, the free trade agreement with the European Union entered into force. A Europe Agreement was signed in June 1995.

The authorities maintained the momentum of structural reforms. In order to consolidate the financial sector, the balance sheets of the two major banks, the Universal Bank of Latvia and the Latvian Savings Bank, were strengthened. In the context of tighter banking supervision, nine banks had their licences withdrawn in 1994. In November, the authorities launched auctions for the privatization of 68 large enterprises, which had been delayed pending the settlement of property rights issues.

The IMF stand-by programme for the period December 1993 to March 1995 remained on-track. The Latvian authorities and the IMF reached an agreement on a new stand-by arrangement for a 13-month period which the IMF board approved in April 1995, for an amount of 27,45 million SDR (about USD 41 million). As in the case of Estonia, however, it is not expected that the authorities will make use of this facility, unless their level of reserves becomes tighter.

## Lithuania

Structural reforms in Lithuania had already started in February 1991, when firms were allowed to raise their prices within certain limits. By early 1992, most prices had been freed. Privatization was also initiated in 1991. Vouchers were distributed in April, and the auctioning of small firms started in September of that year. In spring 1992, Lithuania left the rouble zone and issued a temporary currency, the talonas. In July 1993, a new currency, the litas, was introduced. However, reforms were slower in other areas, in particular in macroeconomic stabilization, external trade liberalization and the financial sector. Deregulation and the shift within the price structure led to high inflation which peaked in 1992 at a 720% (average) level. Monetary policies, however, were tightened in spring 1993 and a sound management of the State budget, which was kept in surplus, allowed inflation to decrease in 1993 (190%, year average).

After several years of recession, GDP stabilized and rose slightly in 1994 (+ 2% estimate). In April 1994, the government introduced a currency board arrangement, according to which the money in circulation is constrained by the amount of hard currencies held in the Bank of Lithuania. The litas is pegged at a fixed rate of four litas to one US dollar. This was a major step in the stabilization of the economy. Monetary growth under the new arrangement was kept moderate and inflation further decreased to 45%. The 1994 State budget was in deficit of about 3% of GDP owing to lower-than-expected government revenues, particularly over the first six months. The slow registration of newly established private sector firms as well as delays encountered in the transition from a general excise tax to a value-added tax explain this poor revenue performance. External trade was further liberalized in May, when the authorities suppressed import tariffs on several goods: by that time, two thirds of imports were zero-rated, while most of the other imports carried a 10% rate. In July, however, import tariffs on a wide range of agricultural goods were raised to an average level of 40%. The share of the West in the country's external trade is continuing to increase. About 50% of Lithuania's exports are now directed to Western markets. Lithuania's trade and current account have been in deficit since 1993. In 1994, the current account recorded a USD 375 million deficit (i.e. 0,4% of GDP). Owing to substantial public and private capital inflows, this deficit was largely covered by the capital-account's surplus. Foreign exchange reserves, which are all the more crucial under the currency board arrangement, continued to increase and covered about three months of imports by the end of the year. On 1 January 1995, the free trade agreement with the European Union entered into force. A Europe Agreement was signed in June 1995. Lithuania became an associated country to the European Union.

The year 1994 also saw a change in core structural areas. Privatization continued to progress; by September, 76% of all eligible companies, representing 30% of the initial State assets, had been privatized. In December, the Central Bank Law was enacted, and was followed by the adoption of the Commercial Banking Law in early 1995. Performance under the stand-by arrangement agreed with the IMF for the period October 1993 to March 1995 was satisfactory. Following the approval of the government's three-year programme last autumn, aimed at a sustained 5% growth of GDP, the IMF approved on 24 October a 134,55 million SDR (about USD 202 million) extended facility, replacing the current stand-by programme. This should allow Lithuania to build up the necessary reserves and to finance key energy and investment-related imports.

### 3. Implementation of macro-financial assistance

In view of the above, the Commission considers that performance criteria attached to the Community loan facilities have been broadly met by all three countries. The Baltic States have successfully implemented stabilization policies agreed with the IMF, which renewed its support by means of a three-year extended fund facility (EFF) for Lithuania in October 1994, and new stand-by arrangements with Estonia and Latvia, in March and April 1995 respectively.

As signs of an economic recovery in the three Baltic States are accumulating, it is expected that their current-account positions will deteriorate in 1995-96, driven by a high demand for investment-related imports. These countries may therefore experience substantial current account deficits over the next few years and will have to rely heavily on capital inflows. Owing to the expected increasing demand for investment-related hard currency finance in these countries, the Commission, after consulting the Monetary Committee, exceptionally agreed in supplemental Memoranda of Understanding negotiated with the authorities to channel the bulk of the second tranche of the loans through the domestic banking sectors to finance sound projects.

The disbursement of the second tranche of the loans has, however, been delayed. In the case of Latvia and Lithuania, this was due to the Commission's request in early 1994 of further evidence of progress on structural reforms, in particular in the areas of privatization and financial sector reform. In the case of Estonia, which has advanced more quickly on both stabilization and structural reforms, the release of the second tranche was delayed, pending clarification from the authorities on their readiness to channel the bulk of the proceeds of the loans through the banking sector.



## 1. Introduction

During most of 1993, the Bulgarian economy went through a crucial transition phase. Real GDP declined further, the budget deficit deteriorated, domestic bank credit expanded rapidly, the financial discipline of State enterprises weakened and the pace of the ambitious reform and structural adjustment process slowed down significantly. Moreover, the central bank (BNB) managed the exchange rate through sizeable interventions in order to contain the lev depreciation, kept price and trade liberalization and made progress in the field of fiscal reform. As a result of serious policy slippages, weak macroeconomic management and a growing uncertainty on the pace of reform, in 1993 the country was virtually cut off from the international financial support, and was unable to reach an agreement with the IMF on a new stand-by arrangement.

During the last quarter of 1993, the overall economic climate improved significantly due to two major events:

(i) a preliminary agreement was reached with Bulgaria's commercial creditors for a comprehensive debt and debt service reduction programme (DDSR);

(ii) a credible new policy programme for 1994 was formulated;

In April 1994, the IMF approved a global assistance package of USD 421 million (of which USD 97 million as a 12-month stand-by and USD 324 million through the systemic transformation facility). In July, the Bulgarian authorities finalized the debt-reduction arrangement with their commercial bank creditors. In order to enable Bulgaria to meet debt-reduction-related up-front disbursements, the IMF and the World Bank decided in September to augment their financial contribution by USD 225 million.

In the framework of the G24 coordination process, the Community decided in April to reconfirm its commitment of a loan of ECU 110 million.<sup>1</sup> The rest of G24 financial commitments in favour of Bulgaria amounted to USD 88,9 million.

## 2. Macroeconomic performance

The policy programme for 1994 focused on the urgent need to implement a tight fiscal and monetary policy aimed at restoring the domestic and external equilibrium. These policies rather than interventions by the central bank should lead to the stabilization of the exchange rate. The stabilization policy was

associated with an ambitious structural reform programme based on further rationalization and privatization of State assets, a strengthening of financial monitoring of loss-making enterprises, completion of the restitution programme and a more stringent control on access to credit.

Achievements have been mixed. In 1994, the Bulgarian economy stopped shrinking. Real GDP increased by 1,4% (– 2,4% in 1993). Industrial production grew by 4% (– 8,5% in 1993), reflecting a more favourable business climate, the expansion of the private sector and new export opportunities. Agriculture grew by 11% in 1994; in services there was an overall decline. Unemployment declined from 16% in 1993 to around 13% in 1994, reflecting partly the economic turn around and from labour office registration the deletion of a significant number of unemployed who became ineligible for social benefits lists.

Despite a tight monetary and credit policy, significant price fluctuations occurred in 1994 as a result of price liberalization and setbacks to economic policy, particularly exchange-rate turbulences. The year-on-year CPI (consumer price index) inflation reached 121,9% (63,8% in 1993).

In 1994, the government implemented a restrictive fiscal policy, aimed at reining in fiscal deficit and hardening the budgetary constraint facing State-owned enterprises. Nominal non-interest expenditure rose less than inflation, subsidies were cut to around 2 to 3% of GDP and the budget deficit/GDP ratio contracted to 6,7% (15,7% in 1993).

The government's planned incomes policy in 1994 was moderately restrictive, with upper nominal wage ceilings consistent with projected inflation targets. Due to higher-than-expected inflationary pressures, incomes, in particular those in the public sector, declined sharply in real terms.

As regards Bulgaria's external developments, the structural shift in foreign trade towards the OECD (Organization for Economic Cooperation and Development) countries was further consolidated, reflecting the positive impact of association and trade agreements with the European Union and EFTA, the lev devaluation, and low labour costs. In 1994, the trade balance showed a surplus of USD 200 million (against a deficit of USD 900 million in 1993) and the current account was balanced (against a deficit of USD 1,4 billion in 1993).

Foreign direct investment remained extremely low (USD 105 million), despite liberal legislation passed in January 1992. However, official external financing greatly contributed to the replenishment, by the end of the year, of Bulgaria's foreign exchange reserves to around USD 1 billion, equivalent to three months of imports.

<sup>1</sup> COM(94) 118 final, 94/0103(CNC), 21.4.1994.

As regards foreign debt management, the DDSR agreement with the London Club was brought to a close on 28 July 1994. Overall, it is estimated that the agreement reduced Bulgaria's USD 8.2 billion debt to Western commercial banks by 46 to 48%. The up-front costs of the operation (USD 715 million) were partly covered by Bulgaria's hard currency international reserves (USD 474 million) and partly by exceptional official external financing (USD 241 million). Furthermore, in April 1994, a third Paris Club debt rescheduling arrangement was reached between Bulgaria and its official creditors, covering all obligations falling due from the previous rescheduling until 30 April 1995. Following these arrangements, Bulgaria's relations with the international financial community were restored.

### 3. Structural reforms

Despite a number of constraints, policy slippages, political uncertainty and weak management, Bulgaria was successful in maintaining previous policy achievements during 1994, such as price and trade liberalization, current-account convertibility and a liberalized exchange-rate regime.

However, a number of unresolved problems remain as regards enterprise restructuring, privatization and the reform of the financial system.

As regards price liberalization, it is estimated that at present around 90% of all retail turnover takes place under a free price regime. However, price controls are still maintained on several products and services including energy, telecommunications, water supply and transport. Despite several upward adjustments, these administered prices have not kept pace with inflation in 1994. The government is committed to winding-up progressively existing indirect price controls on agricultural products (minimum producer prices, minimum import prices, maximum margins, etc.).

Since 1992, the progress in trade liberalization has been encouraging but uneven. Export prohibitions have been removed and export quotas on some 10 products have been replaced with export taxes. The 3% import surcharge was lowered to 2% in January 1994 but by mid-1994 the government still kept some temporary trade barriers to protect domestic industry and agriculture, in the form of minimum import prices, import licences, etc. Bulgaria's interim Association Agreement with the European Union entered into force on 1 January 1994.

Bulgaria's foreign exchange-rate regime has been liberalized, and was effective from February 1994. Foreign exchange ceilings for current personal payments (tourism, etc.) by residents have been raised significantly and current-account convertibility is ensured for trade-related payments. Some

restrictions on current payments and transfers are, however, still in force.

Significant progress has been accomplished in the field of property restitution which triggered a fast development of a dynamic private retail and trade sector (it now accounts for over 50% of all retail and wholesale trade in the country).

The State enterprise sector is weak and debt-ridden. Budget constraints on enterprises are too soft and credit ceilings by the banking system are circumvented via the accumulation of inter-enterprise arrears (at present they may account for about one quarter of the value of industrial production). In order to tackle these problems, the government's strategy focuses on implementing financial rescue plans, enterprise restructuring and privatization.

A Law passed in December 1993 authorized the government to issue long-term bonds in both domestic and foreign currency aimed at replacing uncollectable, lev- and US-dollar-denominated loans and interest arrears accumulated in banks' portfolios by the end of 1991. Loans to State enterprises will therefore be borne by the government, which eventually might convert them into equity or decide on their write-off or rescheduling as soon as companies are restructured or privatized.

In the field of restructuring, major steps undertaken during 1994 include the formulation by main loss-making enterprises of comprehensive loss-reduction and rationalization plans, and the development of a mechanism to monitor bank credit to these enterprises, with a view to strengthening their financial discipline.

As regards privatization, in 1994 the government was determined to accelerate implementation of the programme by amending the Privatization Law with the aims of facilitating standard market-based privatization via the Privatization Agency, completing small-scale privatization and carrying out, in parallel, a mass privatization scheme involving 500 medium-sized and large enterprises. However, due to the absence of the required political determination by the interim government to carrying out the programme, the implementation of mass privatization has been delayed and privatization through standard methods has proceeded only slowly.

At present the Bulgarian banking system is still affected by a number of constraints, including undercapitalization, inadequate management, insufficient supervision by the central bank on capital adequacy and prudential regulations, a slow privatization process, lack of financial discipline ('easy credit'), fragmentation and a growing number of non-performing loans to enterprises. In order to cope with this highly disturbing situation, several actions were undertaken in 1994. The capability of the Banking Supervision Department at the



Bulgarian National Bank has been strengthened. Two regular full onsite inspections to problematic banks were carried out by mid-1994 and two more were programmed by the end of the year. A bank consolidation programme was completed under the aegis of the Bank Consolidation Company (BCC) so that 66 public sector banks have been merged into 11 major banks. The clean-out of bad loans proceeded but the gradual recapitalization of the banks progressed only slowly owing to its budgetary costs. In 1994, a timetable for a gradual privatization of some banks was prepared and is expected to be carried out by the end of 1995.

#### **4. Implementation of macro-financial assistance**

The disbursement of the ECU 110 million Community loan decided in October 1992 in the framework of G24, as a

complement to the IMF assistance to Bulgaria, was delayed as the 1992 stand-by arrangement with the IMF went off-track. For the same reason, no other G24 assistance was released under this initial package. At the end of 1993, conditions were restored for the resumption of EU/G24 assistance to Bulgaria. Following the adoption of a new IMF stand-by arrangement, on 16 May 1994, the Council of the European Union agreed with the Commission that the 1992 Decision on Community macro-financial assistance to Bulgaria could be reactivated in the context of the new programme. The release of a first tranche (ECU 70 million) took place in December 1994 on the basis of the approval of the new IMF stand-by and the debt-relief arrangement agreed between creditors. The release of the second tranche is conditional upon observance by Bulgaria of standard macroeconomic performance criteria, including a satisfactory track record of the IMF stand-by, a proper implementation of DDSR operation and progress with structural reform.



## 1. Introduction

On 13 June 1994, the Council of the European Union decided to grant Moldova a loan of ECU 45 million with a maximum duration of 10 years<sup>1</sup> to assist the country in its efforts to transform its economy to a market economy and to strengthen the reserve position of the central bank. The Community loan was part of an overall package mobilized by the international donor community in favour of Moldova to complement the resources provided by the IMF and the World Bank.

## 2. Macroeconomic performance

Following the introduction, in November 1993, of its national currency — the Moldovan leu — Moldova has made a decisive turn towards financial stabilization in the context of the economic programme supported by an IMF stand-by arrangement (approved in December 1993) and complementary assistance from the international community, including the ECU 45 million Community loan.

The programme was implemented in a very difficult environment. Real GDP is estimated to have fallen by about 22% in 1994, compared with an anticipated decline of 3%. This is in part attributable to the continuing disruptions to output and trade associated with the collapse of central planning. Industrial production fell by about 30% in the first six months of 1994, before stabilizing in the second half of the year. Furthermore, a severe drought, followed by flooding and hailstorms, devastated key crops in this mostly agricultural country in the third quarter of 1994.

Despite this unfavourable economic environment, the Moldovan authorities demonstrated considerable resolve and consistency in the pursuit of financial stabilization. Reviews under the IMF stand-by arrangement were successfully completed in June and December 1994, and all performance criteria for the end of December 1994 were met. The key objective of the programme was a rapid and sustained reduction in the rate of inflation based on the introduction of the leu, and stabilization of the exchange rate. As a result of the firm implementation of the programme, inflation decelerated sharply in 1994. The monthly rate of inflation fell from an average rate of about 20% in the fourth quarter of 1993 to an average rate of about 3% in the fourth quarter of 1994. As inflation subsided, the exchange rate stabilized and the credibility of the leu was enhanced (as reflected by the reversal of currency substitution), allowing a decline in nominal and real interest rates.

The fiscal deficit for 1994 was contained to 8% of GDP, despite the greater-than-envisaged decline in real output and inflation. However, liquidity problems in the enterprise sector impeded tax collection and resulted in the assumption by the government of guaranteed loans to enterprises in default. Furthermore, expenditure arrears rose by approximately 1.5% of GDP, including arrears on wages, as a result of the application of a strict cash management system.

The balance of payments remained under severe pressure throughout 1994 primarily as a result of higher prices for imported energy and the effects of natural disasters. Based on preliminary data, the current-account deficit was equivalent to 9% of GDP. Moldova was highly dependent on foreign assistance, the disbursement of which covered some 50% of total imports. The IMF and the World Bank contributed some 56% of total foreign assistance, and other bilaterals some 44%, including the European Union (ECU 25 million corresponding to the first tranche of the macro-financial assistance), Japan (USD 30 million), the USA (USD 20 million) and Romania (USD 10 million). Furthermore, arrears to Russia, mostly by Moldovan enterprises for energy imports, reached the equivalent of USD 120 million. With the pace of disbursements in foreign assistance increasing late last year, the gross reserves of the central bank reached the equivalent of three months of imports at end-1994.

At this critical juncture of the stabilization process, the Moldovan authorities have formulated an ambitious strategy for 1995 with the objective of consolidating the progress in stabilization and intensifying structural reforms. The programme, which is supported by a new IMF stand-by arrangement approved in March 1995, requires further complementary financing from the international community.

The programme aims at economic growth of 1.5%, led by a recovery in the agricultural sector with the return of normal weather conditions, a reduction in the annual rate of inflation to about 10% and the containment of the deficit in the current account of the balance of payments. To these ends, fiscal policy is centred on sharply reducing the budgetary deficit to the equivalent of 3.5% and monetary policy is to remain tight.

In the first quarter of 1995, the Moldovan authorities have strictly implemented the financial policies contemplated in their programme. Based on preliminary data, all performance criteria for the end of March have been met, including a better-than-expected foreign exchange position of the central bank. This has resulted in a stable exchange rate and a containment of inflationary pressures.<sup>2</sup>

<sup>1</sup> Council Decision 94/346/EC of 13 June 1994.

<sup>2</sup> Monthly inflation rate average of 2.5% in January and February, slightly exceeding the target rate due to the temporary growth of reserve money at end-1994 (resulting from the bunching of disbursement of external assistance) and the effect of the liberalization of prices in neighbouring Ukraine.

### 3. Structural reforms

The progress made in terms of structural reform in 1994 was mixed. State enterprises remained largely unresponsive to market forces (which resulted, *inter alia*, in the increase in arrears to the budget and to external suppliers of energy as indicated above), due, in part, to the weakness of the bankruptcy and liquidation process, and delays in privatization. However, towards the end of the year, there was a substantial acceleration of reform efforts, as the authorities recognized that further delays in implementing structural reforms threatened to undermine the stabilization gains. A new streamlined auction procedure was introduced that facilitated the implementation of an ambitious schedule for the auction of State enterprises. The government also decided to identify and initiate liquidation proceedings against seven of the most problematic State enterprises.

The acceleration of structural reforms in late 1994 is to be sustained in 1995 through an accelerated privatization programme, the establishment of the legal basis for bankruptcy proceedings, the strengthening of the capital base of the banking system and the development of indirect market-based monetary controls.

The acceleration of the reform efforts that started in the last quarter of 1994 has continued in 1995. In particular, a new ambitious privatization programme covering 1995 and 1996 has been approved by the Parliament on 15 March, which covers a substantial portion of the remaining State assets, and introduces, alongside the existing voucher system, privatization for cash (in order to provide new liquidity to enterprises for post-privatization restructuring and to open privatization to foreign investors). The pilot liquidation of seven enterprises is now well under way; the Liquidation Committee, that performs asset sales and the payments of creditors, has been formed, and five of these enterprises have been liquidated. The liquidation of further 15 enterprises through the same procedure is contemplated before the end of June. A Bankruptcy Law has been prepared; a new draft law to approve prudential regulation and ensure the autonomy of the central bank is at present before Parliament; and action plans to ensure capital adequacy for 10 problematic banks were agreed by the central bank in January.

### 4. Implementation of macro-financial assistance

The Community loan of ECU 45 million decided on 13 June 1994 was to be disbursed in two tranches, upon fulfilment of the macroeconomic conditions attached to it. The first tranche, of ECU 25 million, was disbursed in December 1994, on the basis of the successful completion of the first programme review under the IMF stand-by arrangement. The disbursement

of the second tranche, of ECU 20 million, was conditional upon a successful track record of the IMF stand-by arrangement and subject to a positive evaluation by the Commission of performance criteria and of progress made with respect to structural reform in the areas of price, trade and foreign exchange liberalization, privatization, and financial discipline of enterprises and the financial sector.

Progress has been substantial in these different areas. Prices of goods and services were fully liberalized in the course of 1994, with the exceptions of energy products, housing rent, telecommunications, public transport, communal services and the State procurement price for grain. Subsidies on agricultural products were eliminated in May 1994, whereas energy subsidies were removed and replaced, for the most vulnerable groups of the population, by a cash compensation system.

Trade liberalization has advanced considerably: all export quotas were removed with the exception of grain and grain products. By end-1994, Moldova lowered its maximum import tariff to 50%, with the exception of a small number of luxury goods, primarily wine products and consumer electronics. Import tariffs were reduced to no more than 30% on 1 April 1995 and a further reduction is expected by end-1995.

In the area of foreign exchange arrangements, authorization was granted to non-residents in July 1994 to repatriate profits and the proceeds of liquidation of their enterprises; also, the foreign exchange surrender requirement for export earnings by enterprises was eliminated in November 1994. Interbank foreign currency exchange has been established, where residents can purchase foreign exchange for most current payments and non-residents can purchase foreign exchange to repatriate earnings.

In the area of privatization, the process was slower than expected but accelerated during the last months of 1994, so that, by the end of December, 304 medium-sized and large enterprises and 273 small enterprises had been privatized, representing 25% of total State assets. The 1995-96 privatization programme was approved by the Parliament on 15 March 1995, whereby two thirds of State assets will be privatized by end-1996.

Regarding the reform of the banking sector, the National Bank of Moldova (NBM) is working on the new regulations that meet the standards set by the Basle Committee. The new regulation binding the commercial banks to classify their portfolio and establish provisions for bad loans has been recently approved. A new draft Banking Law has been prepared and submitted to the Parliament. This law provides for the independence of the NBM in conducting monetary policy, as well as for the additional rights of the NBM in supervising

and controlling the activities of commercial banks. The new draft Banking Law also provides for penalties in case of infractions to prudential regulations.

In view of the measures taken and commitments for further action provided by the Moldovan authorities, the conditions attached to the disbursement of the second tranche of the Community loan are considered to be met.

In order to ensure a sustainable balance-of-payments situation in 1995, further macro-financial assistance in favour of Moldova to complement the resources provided by the IMF and the World Bank will be necessary, as was recognized by the international donor community in the framework of the Consultative Group meeting organized by the World Bank in March 1995. Following the disbursement of the second tranche, the Commission intends to present a proposal for further macro-financial assistance to Moldova of up to ECU 15 million.



## 1. Introduction

In the course of 1993, inflation accelerated in Romania in the wake of substantial price liberalizations. A lax monetary policy and a lack of financial discipline in State-owned enterprises (SOEs) further fuelled inflation to over 300%. Interest rates were steeply negative and resulted in a flight of the leu into foreign currency holdings. The National Bank of Romania (NBR) continued to administer the official rate and multiple exchange rates persisted, with the gap between the official and the (private) exchange bureaux exchange rate reaching more than 50% by the end of the year. NBR foreign reserves shrank to less than USD 50 million by end-1993, equivalent to three days of imports, while commercial banks held some USD 1 billion in foreign assets. Very little was achieved in the areas of SOE restructuring and privatization. Despite some progress in fiscal reforms and a reduction of the fiscal deficit to 2% of GDP, the IMF was not in a position to continue its financial support to Romania in 1993 and no complementary EU/G24 macro-financial assistance could be mobilized either.

Only in December 1993 did the authorities reach an understanding with the IMF on a new economic programme for 1994-95. In May 1994, the IMF board approved this programme and the accompanying financing facilities (stand-by and structural transformation facility) for an amount of USD 700 million, following EU/G24 financing assurances for the residual gap.

## 2. Macroeconomic developments

The main objectives of the 1994-95 programme are to reduce annual inflation to around 70 to 75% by the end of 1994 and to diminish significantly the current-account deficit. To achieve these objectives, the authorities pledged to increase interest rates to positive levels in real terms, to liberalize the exchange-rate regime, to limit the fiscal deficit to 2,5% of GDP in 1994 and to speed up privatization and financial restructuring of State-owned enterprises.

Monetary policy was tightened towards the end of 1993, when the NBR started to auction part of its refinancing credits at market-determined interest rates. This resulted in a general increase in interest rates throughout the banking system to positive levels in real terms. The average cost of NBR refinancing rose to more than 12% per month in early 1994, at the time when inflation rates fell to 5 to 8% per month. Nominal interest rates started to decline again slowly in the second and third quarters of 1994, in line with inflation. The average NBR refinancing rate decreased to around 5% per month at the end of 1994, when inflation had slowed down to around 2% per month. Interest rates practised by commercial banks followed a similar pattern.

The increase in interest rates renewed confidence in the leu and narrowed the gap between the official exchange rate, fixed by the NBR, and the rate in the private exchange bureaux. After a nominal depreciation of some 14% in February and March 1994, the NBR abandoned the administered exchange-rate regime and switched to a market-determined exchange rate in early April. An interbank foreign exchange market was established in August. However, in the third quarter of 1994, a significant gap between official and private bureaux exchange rates reoccurred and persisted throughout the first quarter of 1995, although these decreased at a slow pace. This indicated that the foreign exchange market was not functioning in a fully transparent way and that the official exchange rate was not fully market-clearing.

The consolidated fiscal deficit actually showed a small surplus for the first five months of 1994. However, this situation was not sustainable as expenditure was artificially held down until May 1994 because the new Budget Law had not yet been approved by Parliament. By the end of the year, the fiscal deficit had reached ROL 2 070 billion or 4,4% of GDP. This was in line with the nominal deficit criteria set out in the programme with the IMF. As a percentage of GDP, it exceeded the initial programme objective because of the stronger-than-expected slowdown in inflation that led to a downward revision of nominal GDP estimates for the year.

Tax reforms continued in 1994 with the introduction of new profit tax, local tax and land tax laws and increased excise duties. Monetary financing of the fiscal deficit through NBR credits to the government was almost completely phased out between March and November 1994. However, a strong increase reoccurred in December of that year when the government reverted from the commercial banks to the NBR to finance part of its deficit.

Strict monetary and fiscal policy resulted in a rapid decrease in inflation, from over 300% per year in November 1993 to less than 62% per year at end-1994, which was considerably below the target of 75% in the IMF programme. The authorities have now set a new annual target for 1995 of 25%, rather than the 40% initially envisaged in the programme.

The current-account deficit was considerably reduced, from USD 1,2 billion in 1993 to USD 0,3 billion in 1994. This was due to a strong export performance (+ 23% in US dollar terms), driven mainly by the depreciation of the leu and by substantial payment arrears and delays in the domestic market that encouraged enterprises to sell abroad. Imports increased by approximately 5% only. Towards the end of 1994 and in early 1995, current-account pressures emerged again, partly as a result of the appreciation of the leu in real terms.

The capital account showed a marked increase in private direct and portfolio investments, reaching USD 414 million, compared with USD 14 million in 1993. However, a slowdown has been registered in loan disbursements compared to the timing in the programme. As a result, the capital-account surplus in 1994 remained below the programme target.

Official foreign exchange reserves, that were almost depleted at the end of 1993, increased to more than USD 620 million (1,2 months of imports) by mid-October 1994. However, in the wake of the reoccurrence of the exchange-rate gap and the authorities' apparent willingness to keep the official exchange rate below the market-clearing level, the NBR sold part of its reserves. They fell to less than USD 407 million at the end of February 1995, when the NBR resumed the purchase of foreign exchange. Foreign exchange holdings in the overall banking system increased from USD 0,9 billion in January to USD 2 billion in December 1994.

### 3. Structural reforms

Imposing financial discipline on arrears- and loss-making State-owned enterprises is a key objective in Romania's 1994-95 economic stabilization programme. However, inter-enterprise arrears increased to approximately ROL 7 billion or 14% of GDP by end-1994. Almost half of these arrears are accounted for by some 70 companies and *régies autonomes* which have been targeted for strict financial surveillance. This includes isolation from the banking system, negotiation of conciliation agreements with their creditors, and drawing-up and implementation of financial recovery plans. If no conciliation could be reached, commercial insolvency procedures would be activated. Liquidation is, of course, not a realistic solution for most of the public utilities and viable financial recovery programmes would have to be established.

Parliamentary approval of the long-overdue Commercial Insolvency Law came in March 1995. This law is a key element in the financial recovery strategy as it defines the proper legal framework for out-of-court conciliation procedures between creditors and debtors. It will permit the initiation of bankruptcy proceedings, while allowing sufficient flexibility for rescue operations.

The privatization of State-owned enterprises has not made much progress. At the end of 1994, three years after the

approval of the Privatization Law, fewer than 900 out of nearly 6 300 State-owned companies had been fully transferred to private ownership. Most of these were small companies, privatized through management-employee buy-outs. A new mass privatization programme was announced by the government in June 1994 with the aim of privatising another 3 000 enterprises by June 1995. However, this programme was only approved by Parliament in March 1995. It was foreseen that at least two of the five major State-owned banks should be prepared for privatization in 1995, but only one bank has so far been nominated, the Romanian Development Bank.

### 4. Implementation of macro-financial assistance

Following Romania's agreement in principle with the IMF on a new programme for 1994-95, the authorities requested the European Union and the G24 to grant further macro-financial assistance to Romania to cover the residual external financing gap of USD 275 million under the 1994-95 programme. Commitments by the European Union/G24 reached some USD 219 million or nearly 80% of the residual gap. This includes further EU macro-financial assistance for an amount up to ECU 125 million, in two tranches, decided by the Council on 20 June 1994.<sup>1</sup> In December 1994, the Commission agreed with the Romanian authorities on the macroeconomic conditions attached to the disbursement of the loan.

However, by May 1995, the first tranche of ECU 55 million had not been disbursed because of slippages in Romania's exchange-rate policy that occurred in the last quarter of 1994 and the first quarter of 1995. The Commission has, on several occasions, expressed concern to the Romanian authorities over these slippages and emphasized the need to re-establish a unified exchange rate at a fully market-clearing level before disbursement procedures can be activated.

The disbursement of the second tranche is linked to the effective implementation of specific structural reform measures, which include progress in privatization, financial restructuring of loss-making enterprises and banking sector reforms, agreed upon with the Romanian authorities in a Memorandum of Understanding.

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<sup>1</sup> Council Decision 94/369/EC of 20 June 1994.



## 1. Introduction

The dissolution of the Czech and Slovak Federal Republic (CSFR) on 1 January 1993 had several negative implications for the Slovak economy at a time when it was still suffering from the shock associated with the dismantlement of the Council for Mutual Economic Assistance and from the difficulties accompanying the transition to a market economy. In particular, the dissolution of the Federation implied the loss of substantial fiscal transfers from the Czech lands, which contributed to the emergence of high budget and current-account deficits in 1993. In addition, the division of the CSFR disrupted trade with the Czech Republic, restricted Slovakia's access to the international capital markets, and was followed by speculation against the Slovak crown which practically depleted Slovakia's official foreign exchange reserves.

In this context, the Slovak Government agreed with the IMF in mid-1993 on a macroeconomic stabilization programme for the rest of that year, which was supported by the approval in July 1993 of a first purchase to the amount of 64.4 million SDR (about USD 100 million) under the IMF's systemic transformation facility (STF). In addition, the World Bank granted Slovakia a USD 80 million economic recovery loan in November 1993.

In July 1994, the IMF approved a 20-month stand-by credit and a second purchase under the STF totalling 180 million SDR (or about USD 280 million), in support of a more comprehensive economic programme for 1994-95. In parallel, the World Bank began discussions on a possible enterprise and financial sector adjustment loan (EFSAL). The macro-financial assistance and programme agreed with the international financial institutions aimed at strengthening Slovakia's delicate balance-of-payments position and at supporting the country's transformation into a market economy following the shock associated with the dissolution of the CSFR.

In support of this programme, the Council of the European Union adopted on 22 December 1994<sup>1</sup> a Decision making available macro-financial assistance to Slovakia in an amount of up to ECU 130 million, as part of a G24 initiative to respond to the request by the Slovak authorities for complementary assistance (in the amount of USD 300 million). Other members of the G24 (mainly Japan, Austria and Switzerland) made further commitments amounting to USD 87.3 million.

## 2. Macroeconomic developments

All macroeconomic variables have been evolving favourably since the second quarter of 1994. Following four consecutive years of recession, the Slovak economy recovered strongly in 1994, with real GDP growing by 4.8% and industrial production by 7%. The recovery of GDP was driven by a strong expansion of net exports, which more than offset a new decline in domestic demand. The unemployment rate, for its part, has stabilized, although at a relatively high level of about 14.5% (it stood at 14.6% in March 1995). GDP is projected to grow again by about 4% in 1995 as domestic demand replaces net exports as a source of growth.

Year-on-year CPI inflation declined from 25% in December 1993 to 11.3% in March 1995, and the government's programme aims at further reducing it to 8% by end-1995. Wage growth, by contrast, accelerated in 1994, with real wages in the industrial sector growing by 7% after declining in 1993. The government, however, has decided to abolish the tax on excessive wage increases introduced last year.

Substantial progress was made in 1994 in reducing the budget deficit. The deficit of the general government closed the year at 2.7% of GDP, down from 7.6% in 1993. The budget for 1995 is consistent with a general government deficit of around 3% of GDP. Monetary policy was also tight in 1994. The net domestic assets of the banking system expanded by only 2%, compared with the 5.5% growth that had been programmed and with an 11.1% growth in 1993. The money supply, however, grew faster than programmed, reflecting the rapid expansion of net foreign assets, which was in turn a consequence of the turn around in the balance-of-payments position. The NBS will continue to conduct a prudent monetary policy in 1995. It has decided to maintain until end-1995 the individual credit ceilings on banks introduced in February 1994, and will aim at a 4.5% growth of net domestic assets and a 12.3% growth of M2 in 1995.

The balance of payments has experienced a clear improvement since the second quarter of 1994. The current account swung from a deficit of USD 0.6 billion (5.4% of GDP) in 1993 to a surplus of USD 712 million (6% of GDP) in 1994. The main factors behind this improvement seem to be the decline of domestic demand, the devaluation of the Slovak crown (including within the bilateral clearing system) and the imposition of the 10% import surcharge in March 1994.

The improvement in the current account has been particularly marked *vis-à-vis* the Czech Republic, with the bilateral balance reaching a USD 806 million surplus in 1994. The turnaround in Slovakia's current account *vis-à-vis* the Czech Republic has been reflected in the balance of the bilateral ecu clearing account. Following a substantial deficit position for Slovakia in

<sup>1</sup> Decision 94/939/EC of 22 December 1994.

late 1993 and early 1994, the account has been showing a Slovak surplus, with the Czech Republic consistently exceeding the ECU 130 million credit limit beyond which payments must be settled in hard currency.

The capital account has also improved. About USD 295 million of official macro-financial assistance (IMF, World Bank's economic recovery loan and Japan Exim Bank) have been disbursed since mid-1994. In addition, the NBS issued in July 1994 a USD 250 million bond in the Samurai market. Foreign direct investment (FDI) increased from about USD 100 million in 1993 to USD 184 million in 1994, although it remains low (1,5% of GDP). Finally, the tight management of interbank liquidity by the NBS, in combination with the perceived stability of the Slovak crown (and, in the first half of 1995, the expectation of a revaluation against the Czech crown), has led to some short-term capital inflows.

These favourable trends in both the current and the capital accounts have been translated into a substantial increase in reserves. Official foreign exchange reserves rose from USD 415 million at end-1993 to USD 2,2 billion in April 1995, or about three months of imports.

In April 1995, the US rating agency, Standard & Poor's upgraded Slovakia's rating from BB- to BB+, or just one notch below the investment grade category. Moody's is also considering an upgrading of its rating to Slovakia. All this should have a positive impact on the country's access to the international capital markets.

Following a 10% devaluation in July 1993, the exchange rate of the Slovak crown has been kept stable against a basket of Western currencies. In July 1994, the number of currencies in the basket was reduced from five to two (the Deutsch mark and the US dollar). In December 1993, the Slovak crown and the Czech crown were, respectively, devalued by 5% and revalued by 3% within the clearing system. However, the 3% revaluation of the Czech crown was reversed in March 1994, and in mid-May, in response to growing speculation on a revaluation of the Slovak crown within the clearing system, the devaluation of the Slovak currency was reduced from 5 to 1%.

### 3. Structural reforms

The Slovak authorities announced in spring 1994 a plan to accelerate privatization based on a greater reliance on voucher privatization. As of the end of August 1994, about SKK 65 billion worth of equity had been designated for inclusion in the second wave of voucher privatization, and between September and November 1994 about 3,5 million citizens (out of a total of 3.8 million eligible citizens) had registered to buy vouchers.

The political stalemate following the 30 September/1 October general election, and the redefinition of the privatization strategy by the new government, resulted in a significant delay of the privatization process. The newly elected Parliament invalidated some direct-sale privatization contracts concluded by the interim government after 6 September 1994, and the voucher scheme has been significantly scaled-down and delayed. The emphasis is expected to be switched back from voucher to standard methods. Priority will be given to direct sales to strategic investors, including sales through instalments to managers and employees.

In the area of banking sector reform, new stricter regulations on the classification and provisioning of bad loans came into force in March 1995. The Slovak Parliament is expected to pass by mid-1995 amendments to the tax laws granting full tax deductibility for bad-loan provisions made by banks during 1995-97. Banks wishing to temporarily benefit from the full tax deductibility of provisions will have to commit themselves to a restructuring programme approved by the NBS, will not be permitted to distribute dividends for several years and will have to make substantial efforts to reduce or keep in check operational costs (including wages). It is also hoped that the ongoing strengthening of the Slovak economy will have some positive effect on the problem of non-performing loans.

The authorities are studying the possible introduction of a deposit insurance scheme, and are preparing changes in the NBS and Commercial Bank Acts aimed at strengthening the supervision and intervention powers of the central bank.

Following abuses and irregularities by certain investment privatization funds (IPFs) and investment companies, the Ministry of Finance has restricted the operations of several of them and is planning to tighten their regulation. The legal amendments being prepared would aim at increasing the transparency and control of their activities, and at better protecting the interests of the shareholders of the IPFs. There is, however, some concern that the amendments may also limit the IPFs' role in corporate governance.

The Ministry of Economy has placed under liquidation 168 State-owned enterprises that are under its jurisdiction, although the process has been completed for only 12 of them. The appointed State liquidators are having difficulty in selling their assets, largely due to the excess supply in the real-estate market. In addition, the authorities are preparing amendments to the Bankruptcy and Conciliation Law aimed at some existing deficiencies and permitting a more speedy resolution of cases.

The government is committed to making the crown fully convertible for current-account purposes by 1 January 1996. Consistent with this, the NBS raised the foreign exchange travel allowance by two thirds (to the equivalent of USD 500

per year per person) as of 1 January 1995. The Czech-Slovak clearing system is expected to be terminated in the second half of 1995. In May 1995, the Czech Government decided to request formally its elimination.

In addition to their plans to introduce full current-account convertibility by 1 January 1996, the authorities are envisaging the liberalization of several types of capital outflows and inflows, and, in particular, outward direct investment, which is still subject to authorization by the NBS. The NBS is finalizing a new Foreign Exchange Act that will provide the appropriate regulatory framework for both the introduction of full current-account convertibility and the partial liberalization of capital movements.

Despite the clear improvement in the current account and balance of payments, the Slovak authorities announced their intention in early 1995 to maintain until end-1996 the 10% import surcharge introduced in March 1994. The current government plan implies the reduction to 7.5% of the surcharge by end-1995 and its gradual elimination in the course of 1996 provided that the balance-of-payments position remains satisfactory. In justifying their decision, the Slovak authorities argue that the expected recovery of domestic demand, the planned introduction of full current-account convertibility and the liberalization of some capital outflows could negatively affect the balance of payments in 1995 and 1996.

Most prices have been liberalized. The share of items that still have regulated prices represents only about 5% of total turnover. These items include energy (electricity, gas and heating, petrol), water, pharmaceutical products, rents, telephones and telegraphs, and public transportation. Prices for electricity (particularly those paid by households), gas and heating are significantly below their economic cost-recovery

levels. Electricity and gas tariffs have hardly been adjusted since 1991. By mid-1995, the authorities are expected to present a plan to bring these prices gradually close to their economic cost-recovery levels in the coming years.

#### **4. Implementation of macro-financial assistance**

The programme agreed with the IMF for 1994-95 remains on-track. Although the implementation of some of the structural reform conditions has been delayed, all the macroeconomic targets and quantitative performance criteria have until now been met. Given the improvement in the balance of payments, however, the Slovak Government has announced that it will not draw, for the time being, on the remaining tranches of the stand-by credit.

In the first half of 1995, the Commission held preliminary discussions with the Slovak authorities on the economic policy conditions to be related to the implementation of the EU macro-financial assistance. In this context, the Commission emphasized that, in view of the favourable developments in the external account, the situation was propitious to start implementing a phasing-out of the 10% import surcharge without further delay. The Commission also insisted on the importance of continued progress in the area of structural reform, in particular with respect to privatization, enterprise restructuring and banking sector reform.

Regarding the disbursement of the complementary macro-financial assistance committed by other G24 members, Japan released its USD 60 million assistance in early May 1995. This was done in the form of a loan from the Japanese Exim Bank co-financed with the World Bank's economic recovery loan.



## 1. Introduction

In autumn 1994, following the election of President Kuchma, the Ukrainian authorities took a major step towards transforming their economy into a market-based one. This came after three years, during which economic policy had been almost totally paralysed by political deadlock and widespread scepticism about market-oriented reform. In a radical change of course, the authorities adopted a bold and comprehensive programme of economic stabilization and reform which was supported by an IMF arrangement under the systemic transformation facility (STF) approved in October 1994 and a stand-by arrangement approved in April 1995, as well as a rehabilitation loan from the World Bank approved in December 1994.

On 22 December 1994, the Council of the European Union decided<sup>1</sup> to make available macro-financial assistance in the form of a 10-year loan of up to ECU 85 million to support Ukraine's adjustment and reform process. This assistance was understood to be complementary to that provided by the international financial institutions as well as by other bilateral donors. The EU loan was made conditional upon agreement between the IMF and Ukraine on a stand-by arrangement and the rapid implementation of the EU/G7 nuclear safety action plan for the closure of Chernobyl. In addition, it was understood that the mobilization of macro-financial assistance for Ukraine would require that the country fully and timely fulfilled its financial obligations towards the Community and that burden-sharing with other bilateral donors is satisfactory.

## 2. Macroeconomic performance

The Ukrainian stabilization and reform programme was adopted in a very difficult environment. With the move of energy prices towards world market levels starting in 1992, Ukraine had suffered severe periods of trade shocks. Given the heavy dependence of its production on energy, Ukraine was forced to reduce import volumes both for energy and other goods, adding further to the economic decline. Following a 38% decline of real GDP in the period 1990-93, output contracted by another 23% in 1994. The impact of the output collapse of the official economy was only partly offset by the rapid growth of the informal sector. In 1994, the current-account balance deteriorated further to a deficit of USD 1,1 billion, with the accumulation of external arrears providing the financing for the balance of payments in the first three quarters of the year. Although inflation had been reduced substantially in the course of 1994 from record levels observed in 1993, the renewed relaxation of financial policies in summer 1994 had created potential new inflation pressures.

Under these difficult circumstances, the Ukrainian authorities made substantial progress with economic stabilization in the fourth quarter of 1994; all quantitative financial targets for end-1994 under the STF were observed, each by a significant margin. A major tightening of the budget was implemented bringing the deficit in 1994 down to 8,6% of GDP and limiting monetary financing of the government in the fourth quarter to 5% of GDP. The bulk of fiscal adjustment relied on the expenditure side, in particular through sharp reductions in subsidies to coalmines, agriculture and communal services. Monetary conditions were also tightened. In late October, commercial credit to the non-government sector was frozen for the remainder of 1994 and the central bank's refinancing rate was significantly increased. At first, the impact of these measures on inflation was not apparent given the inflation potential in the economy and the liberalization of prices undertaken as part of the reform programme. Monthly inflation rates in the order of 2 to 3% in summer 1994 increased sharply up to a maximum of 72% in November 1994. Since then, there has been a continuous decline of inflation — down to a monthly rate of 5,8% in April 1995.

The balance of payments remained very tight throughout 1994. In the last quarter of 1994, Ukraine received foreign assistance from international financial institutions, as well as contributions and pledges from bilateral donors to fill the residual financing gap (after contributions of IFIs are accounted for) estimated at USD 600 million. Apart from the rescheduling of arrears by Russia and Turkmenistan (some USD 350 million), bilateral contributions reached some USD 200 million, including a USD 70 million contribution from the USA and USD 5 million from the Netherlands. As a consequence, Ukraine was able to remain up to date with payments for imports. It also settled part of payment arrears. Official international reserves increased somewhat, but with two weeks of imports at the end of 1994, the level remained low.

At this difficult juncture of the stabilization process, the Ukrainian authorities decided to continue and enhance their ambitious stabilization and reform programme in 1995 in the context of an IMF stand-by programme (providing Ukraine, together with the second tranche of the STF, with some USD 1,9 billion). Other bilateral donors (including Russia, the USA, Japan, and the European Union) are providing complementary assistance.

The programme for 1995 aims at bringing monthly inflation down to 1% in December 1995. One important element in this strategy is the sharp reduction of the State budget deficit to 3,3% of GDP. Budgetary expenditure will be generally reduced by over 10% of GDP compared with its 1994 level, except for social expenses and subsidies to households which will be increased from 6,2 to 8,5% of GDP. The National Bank of Ukraine has adopted a monetary programme that is consistent with this budget and with the objective of lower inflation.

<sup>1</sup> Decision 94/940/EC of 22 December 1994.

In the first quarter of 1995, the Ukrainian authorities have implemented the financial policies envisaged in their programme. This has resulted in a containment of inflationary pressures and a stabilization of the exchange rate. All performance criteria for end-March were met, except for those relating to the accumulation of arrears.

### **3. Structural reforms**

The Ukrainian authorities have also launched a programme of ambitious structural reform, even though much remains to be done and several actions subject to structural benchmarks under the STF were postponed. Under the programme, the authorities advanced rapidly towards full price liberalization, including the revoking of controls on profit margins. Administered prices set by the State were raised for rents, utility charges, bread and energy products. The government also took a number of steps towards reducing the role of the government, including the formulation of the mass privatization programme for 1995 and the preparation of the elimination of the old system of State orders starting from 1 January 1995. To shelter vulnerable groups from the impact of the adjustment measures, minimum pensions and social benefits were raised.

Liberalization of the foreign exchange market proceeded well in the fourth quarter. The government has already decided to abolish all remaining quotas and licences other than on grain and goods subject to voluntary export restraint (VER) under international agreements. It also intends to abolish quotas on ferrous and non-ferrous metals and on grain by mid-1995. The authorities have substantially reduced the foreign currency surrender requirements for export receipts to 10% and are considering abolishing it completely.

The Ukrainian Government also envisages completing price deregulation to a large extent in 1995 by removing the existing restrictions on price increases by artificial monopolies. Prices of goods and services provided by natural monopolies are being further adjusted thus ensuring a gradual decline in subsidies. A major privatization effort is being undertaken in 1995, aiming at the completion of the privatization of 8 000 medium-sized and large enterprises by the end of the year through vouchers, as well as of 90% of small enterprises. Foreigners will be allowed to participate in cash privatization. The authorities also intend to improve enterprise governance. Bankruptcy procedures are expected to be simplified and land reform will be further pursued.

### **4. Implementation of macro-financial assistance**

The EU loan of ECU 85 million decided on 22 December 1994 was to be disbursed in a single tranche conditional upon an IMF stand-by arrangement and a rapid implementation of the EU/G7 nuclear safety action plan for Ukraine. As of May 1995, with the stand-by arrangement approved and on-track, and substantial progress achieved towards the closure of the Chernobyl nuclear power plant, the Commission intends to proceed rapidly with the implementation of the ECU 85 million loan facility.

In view of the further considerable financing needs of Ukraine in the context of the stand-by arrangement, the European Union is currently considering a second long-term loan in favour of Ukraine that would complement financial assistance from the international financial institutions and other bilateral donors. The Commission adopted a proposal in this respect on 16 May 1995.

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