CENTRAL AMERICA AND MEXICO

Costa Rica

In 2000, GDP rose by around 1.5%, after having grown at a rate of 8% for two years. This was mainly due to the 11% decline in the value of exports and a production lag in the high-technology electronic industry which affected Intel exports. High interest rates and rather adverse expectations discouraged investment and consumption. Real wages in the formal sector remained stagnant and per capita income fell. The urban unemployment rate dropped to 5.3%.

Monetary policy, a smaller nominal devaluation of the exchange rate and a slowdown in production activity helped keep inflation at 10%, despite pressures from rising fuel prices.

The deterioration of the terms of trade, the 7% drop in the value of exports of goods and services, and payments abroad created a current account deficit of 5.1% of GDP. Reduced capital inflows, especially from foreign direct investment (FDI), were insufficient to finance this disequilibrium, and the resulting loss of reserves amounted to US$ 100 million.

The legislature did not pass the structural reforms bill submitted by the executive branch, which provided for improvements in the electrical power and telecommunications utilities and defined the role of the State in that area. The Supreme Court had raised objections to the bill.

Public finance continued to hinder stabilization efforts. The consolidated public-sector deficit, including that of the central bank, amounted to nearly 4%, and the central government deficit totalled 2.6% of GDP.

Current revenues of the central government grew by 8% in real terms, thanks mainly to the application of the Tax Rules and Procedures Code, the elimination of Tax Credit Certificates (CATs) and collections of customs duties. Current expenditures rose by 9%, with transfers to the rest of the public sector, and salaries and wages for teachers and public security employees, playing a major role in this increase. Interest payments, amounting to 26% of current expenditure, represented a heavy burden. Investments by the central government fell by around 20% in real terms.

COSTA RICA: MAIN ECONOMIC INDICATORS

	1998	1999	2000[a]
	Annual growth rates		
Gross domestic product	8.0	8.0	1.5
Consumer prices	12.4	10.1	10.4
Real wages	5.6	4.7	0.7
Money (M1)	12.3	20.6	7.6
Real effective exchange rate [b]	2.7	4.0	0.0
Terms of trade	3.2	-1.1	-7.2
	Percentages		
Urban unemployment rate	5.4	6.2	5.3
Fiscal balance/GDP	-2.5	-2.3	-2.6
Real deposit rate	0.9	3.9	2.2
Real lending rate	9.6	14.3	12.5
	Millions of dollars		
Exports of goods and services	6 884	8 221	7 640
Imports of goods and services	7 047	7 242	7 385
Current account	-495	-692	-775
Capital and financial account	345	1 174	675
Overall balance	-150	480	-100

Source: Statistical Appendix.
[a] Preliminary estimates.
[b] A negative rate indicates an appreciation of the currency in real terms.

Monetary policy was based on transactions in the open market involving the placement of monetary stabilization bonds (BEM). During the first half-year, steps were taken to control the increased liquidity generated by greater international reserves, central bank losses and the use of deposits by the central government.

In March, in order to bring down the cost of credit, the legal reserve requirement was reduced by 2 points and was set at 12%. The 27% ceiling on increases in lending by State banks was eliminated, and incentives were implemented to bring down interest rates, which were reduced by 1.75%. By late September, loans to the private sector had risen by 20%.

As of September, the money supply (M1) had grown more than nominal GDP. Liquidity in local currency (M2) rose by 24%, owing to the growth of quasi-money and of savings and time deposits. The central bank's quasi-fiscal losses drove up its deficit to 2.1% of GDP.

The crawling-peg exchange-rate regime led to an annual nominal devaluation of 7.9%. In real terms, the exchange rate remained stable and did not affect competitiveness. Trade policy relied heavily on a unilateral opening up to the external market; negotiations on trade agreements with Chile, Canada and Panama; regional and hemispheric integration efforts; and negotiations on specific products.

The public-debt policy entailed exchanging high-interest domestic debt for lower-interest external debt. The government placed US$ 250 million worth of bonds on the international market. The central government's domestic bonded debt rose to 23% of GDP. The government made a US$ 257 million payment on its debt with the central bank.

External demand fell as a result of the decline in the volume of exports of Intel products, bananas and sugar. This was partly offset by an increase in tourism-related activities, coffee exports and sales of manufactured products in the country's free zones. Domestic demand fell, as consumption rose by only 1%. Fixed investment was down by 3.3%.

GDP grew by only 1.5%, primary-sector activities and manufacturing declined, and construction stagnated. Other sectors grew on average by 4.3%. Agricultural production fell by 3%, owing to a drop in international prices, financial difficulties experienced by growers and bad weather.

Manufacturing output decreased by 3.1%, especially because of weaker demand for personal computers and production delays in the manufacture of new high-technology electronic products.

Inflation (10.4%) was slightly higher than planned; this was mainly due to factors such as rising fuel prices, problems with the supply of foodstuffs and increases in telephone rates, public transport and alcoholic beverages. Monetary and exchange policy, sluggish growth in consumption and declining investment helped slow down increases in the consumer price index.

Real average wages rose slightly. Urban unemployment fell by 0.9 points, to 5.3%, as the supply of labour fell somewhat; female unemployment in urban areas was 6.4%. The Legislative Assembly enacted the Worker Protection Act, which provides for modernization of the pension system and strengthening of the financial position of pension funds.

The deficit on the balance-of-payments current account rose to 5.1% of GDP. After a decade of growth (18% per year), exports of goods fell in 2000 (-11%) because of poor international prices for coffee and sugar and the drop in sales of Intel semiconductors. Exports of services, particularly in the tourism sector, rose by 10%. Imports of goods rose slightly, as economic activity slowed down and fuel prices rose (41%). Imports of capital goods declined by 2.2%.

Returns on FDI, which had been significant during the last two years, were lower owing to the drop in the profits of high-technology industries. Interest payments

continued to rise and contributed to the increase in the current account deficit.

As regards the capital account, bond placements caused net lending to the public sector to rise by 7%. The policy of attracting FDI, along with favourable conditions in terms of infrastructure, legal provisions, the labour market, fiscal variables and the macroeconomic framework, had led to a substantial increase in investment from the mid-1990s onward, bringing it to an average of US$ 610 million in 1998 and 1999, but in 2000 it fell to a little over US$ 400 million.

Capital inflows were lower than the deficit on current account, and international reserves consequently fell by US$ 100 million.

El Salvador

Economic growth slowed to 2.5% compared with 3.4% in 1999, owing in large part to the adoption of restrictive monetary policies, a less vibrant performance by exports (due to the fall in international prices for coffee and sugar), the rise in fuel prices and the slowdown in construction, agriculture and commerce. Inflation will be slightly above 3%, in contrast with the 1% deflation recorded in 1999. Nominal interest rates on deposits in colones declined; the exchange rate remained stable; the current account balance again showed a deficit, similar to the 1999 figure; and the fiscal deficit widened.

Towards the end of November, the Legislative Assembly adopted the monetary integration act, which, with effect from 1 January 2001, establishes the dollar as the unit of account in the financial system, fixes the exchange rate at 8.75 colones to the dollar and allows the circulation of other currencies.

The most vulnerable sectors were the public financial sector, which deteriorated in comparison with 1999, and the external sector. The authorities maintained a conservative fiscal policy, but tax revenues were at a low ebb. The deficit of the non-financial public sector (NFPS) widened and real public investment grew by just 1%. External public debt was equivalent to 22% of GDP.

Central government finances recorded a deficit equal to 2.5% of GDP. Tax revenues expanded by 7.6% in nominal terms, and the tax burden was 10.5% of GDP, a similar percentage to that of 1999. Exemptions on some agricultural products and medicines were removed. Thus, the tax structure did not vary significantly, the heavy reliance on value-added tax accentuating the procyclical nature of tax revenue.

If receipts remain stagnant, as may be expected from current trends, there is likely to be increased pressure on the fiscal deficit, above all because of the over US$ 1 billion in pensions which the government will have to pay out during the next five years.

Monetary policy was restrictive and was designed to regulate and reduce the excess liquidity on the money market, above all through placement of securities of the Central Reserve Bank.

This measure proved less effective in controlling inflation. Although open-market transactions did function effectively as a contractionary factor, reducing the monetary base in the context of an expansionary fiscal policy, they generated quasi-fiscal costs.

Nominal interest rates on loans and deposits in national currency fell. Real deposit and lending rates also declined as a result of the higher levels of inflation.

EL SALVADOR: MAIN ECONOMIC INDICATORS

	1998	1999	2000[a]
	Annual growth rates		
Gross domestic product	3.5	3.4	2.5
Consumer prices	4.2	-1.0	3.4
Money (M1)	8.6	13.5	-0.8
Real effective exchange rate [b]	-1.5	1.2	0.6
Terms of trade	-2.5	-5.3	-5.6
	Percentages		
Urban unemployment rate	7.6	6.9	6.7
Fiscal balance/GDP	-2.0	-2.2	-2.5
Real deposit rate	7.6	10.2	7.4
Real lending rate	12.2	14.9	11.9
	Millions of dollars		
Exports of goods and services	2 742	3 090	3 490
Imports of goods and services	4 269	4 599	5 170
Current account	-85	-204	-205
Capital and financial account	387	409	210
Overall balance	302	205	5

Source: Statistical Appendix.
[a] Preliminary estimates.
[b] A negative rate indicates an appreciation of the currency in real terms.

Foreign exchange policy since 1993 has been geared towards the fixed rate of exchange; from the mid-1990s, a higher rate of inflation than that of the United States, combined with inflows of remittances, has contributed to a real revaluation of the colón of almost 20%. This has helped to stabilize the economy.

It is hoped that establishment of the nominal exchange rate from January 2001 will reduce the country's vulnerability to speculative attacks and bring interest rates down. This new exchange rate regime will, however, limit the degree of freedom enjoyed by the central bank, as it forfeits its role as lender of last resort and ceases to use monetary policy as a policy tool for dealing with external shocks.

The foreign trade policy focused on international trade negotiations, while maintaining the tariff reduction programme. The free trade treaty between Mexico and the Northern Triangle (El Salvador, Guatemala, Honduras) was signed, and negotiations on the treaty on free trade and protocol with Chile were concluded. In addition, negotiations are continuing with the Andean Community and with Canada. A free trade agreement is being negotiated with Panama on maritime transport services and financial services.

The economy's slow growth since 1996 is attributable to the contractionary monetary policies adopted and to a sluggish performance by the external sector. In 2000, the strongest growth sector was transport, storage and communications (4.6%); this was followed by manufacturing (4.1%), mining and electricity, water and gas (3%); agriculture (2.7%) and construction (2.1%).

Inflation, which had been negative in 1999, rose over 3%, when the removal of government subsidies and the rise in fuel prices resulted in an increase in electricity rates.

Minimum wages remained unchanged between September 1999 and September 2000. In industry, commerce and services, the minimum wage has been maintained at 42 colones per day and in the agricultural sector, at 28.2 colones per day. In construction, the only sector where wages increased, they were raised from 64.02 colones to 71.03 colones per day for skilled workers, and from 52.15 to 57.86 colones per day for less skilled workers. The urban unemployment rate stood at 6.7%, slightly lower than the average for the period 1994-1999 (7.2%).

Performance in the external sector was less favourable than in 1999. The trade balance showed a deficit of US$ 1.7 billion, 11% higher than in the previous year. The current-account deficit was maintained at a manageable level (1.6% of GDP), thanks largely to remittances from family members living abroad, which amounted to US$ 1.58 billion.

The value of merchandise exports strengthened by 13%, owing mainly to exports from the maquila sector (20%). Exports to other Central American countries grew by 10%. Imports were up 14%, with the highest increases being recorded in the maquila industry (20%) and consumer goods (14%). Imports of raw materials also expanded (9%) as did capital goods (9%).

Guatemala

In the first year of the new Administration, Guatemala made progress towards restoration of domestic and external equilibria, which had been threatened by the expansionary fiscal policy applied in the preceding year and by the worsening terms of trade. According to estimates, inflation will have been in the order of 4%, international reserves will be higher, the nominal exchange rate will stabilize, and gross domestic product (GDP) will be up by 3.5%. In May, the Fiscal Covenant was signed, reflecting national consensus on tax reform and rationalization of public resources. In practice, the results have been limited. Lending by banks to the private sector remained sluggish.

In March, the authorities cut back the public budget for 2000 by 10%. Subsequently, the maximum rate of taxation on personal income and profits was raised to 31%, restrictions were placed on deductions for grants and reinvested earnings, the exit tax was increased, and new tax rates were established for alcoholic beverages. The tax burden is likely to have increased by 0.3 percentage point, exceeding, for the first time, 10% of GDP. From the second quarter onward, public expenditure increased, bringing the fiscal deficit to 2.5% of GDP. There were major distortions in the composition of public expenditure, and investment dropped 5% in real terms; nevertheless, consumption is expected to have kept pace with GDP (3.6%). In view of the limited progress made with fiscal reform, the meeting of the consultative group of international donors scheduled for November was postponed, tentatively to 2001.

Monetary policy sought to place the country on a low-inflation path; to that end, an attempt was made to control liquidity through intense participation by the Bank of Guatemala in open-market operations. From January to November, certificates of deposit totalling more than 6 billion quetzales were issued, triple the value obtained in 1999. This resulted in a change in the maturity profile and rates of such certificates. While in January, placements had a maturity of less than 180 days, in October, more than 50% had a maturity of over 336 days. The weighted average nominal interest rate fell six points, bringing the annualized rate to 18% in November. These operations were a means of absorbing excessive increases in the money supply arising from public spending and to the rally in external capital flows. According to official estimates for 2000, liquidity (M2) is estimated to have expanded from 11% to 13%, a percentage that is consistent with established goals.

The high real lending rates (close to 15%) and the persistent problem of non-performing loans, continued to restrict credit to the private sector. The intense placement of bank paper by the Bank of Guatemala may have had the same effect, insofar as the private banking system tended to prefer such certificates. In November, bank lending to the private sector was scarcely 4.9% above the level of 12 months earlier in nominal terms. In 2000, unlike the previous year, the Bank of Guatemala did not grant loans for restructuring to alleviate the problem of non-performing portfolios. It should be noted that such loans did not provide for effective sanctions for non-fulfilment of restructuring goals.

The rate of the quetzal against the dollar fluctuated sharply at the start of the year, reflecting uncertainty about the elections, the worsening terms of trade and the relaxation of fiscal policy in late 1999. Subsequently, the restrictive monetary policy brought stability to the foreign exchange market. The quetzal is estimated to have depreciated by 3% in real terms in the course of the year, as a result of the wide gap in inflation levels between Guatemala and its trading partners.

GUATEMALA: MAIN ECONOMIC INDICATORS

	1998	1999	2000[a]
	Annual growth rates		
Gross domestic product	5.0	3.6	3.5
Consumer prices	7.5	4.9	4.2
Money (M1)	13.5	14.2	29.2
Real effective exchange rate [b]	1.2	14.5	2.3
Terms of trade	- 0.6	- 7.5	-3.8
	Percentages		
Urnemployment rate	3.8	...	...
Fiscal balance/GDP	-2.2	-2.8	-2.5
Real deposit rate	-1.3	2.6	3.7
Real lending rate	9.1	13.6	13.9
	Millions of dollars		
Exports of goods and services	3 467	3 435	3 745
Imports of goods and services	5 030	4 984	5 425
Current account	-998	-1 015	-1 025
Capital and financial account	1 241	890	1 700
Overall balance	243	-125	675

Source: Statistical Appendix.
[a] Preliminary estimates.
[b] A negative rate indicates an appreciation of the currency in real terms.

The authorities pressed forward with structural reforms after signing the free trade treaty between Mexico, El Salvador and Honduras. With effect from 1 January 2001, tariffs and other barriers to trade and intraregional investment were to be gradually dismantled. Sugar, coffee and bananas are not included under this treaty.

With respect to overall demand, the volume of goods and services exports, which expanded by 4.2%, showed the strongest growth, followed by consumption, which increased 3.6%, a similar percentage to GDP growth; conversely, investment declined. The volume of imports rose slightly (1.7%). A 9% contraction in public investment was attributable to efforts to correct the fiscal deficit and, to some extent, to the typical delay in the start-up of new projects in the first year of any administration. The decrease in private investment was attributable to the uncertainty associated with the transition to a new government and to the credit squeeze. Questions in certain political circles as to the legitimacy of the privatization processes also perturbed the investment climate. At the sectoral level, the following sectors recorded a sharp fall in their contribution to GDP: construction (-12%) and mining (-5.1%); on the other hand, both manufacturing and agriculture recorded a moderate expansion (2.3% and 3%, respectively).

Inflation rose in the first quarter of the year, reflecting the increase in oil prices, telecommunications rates and wages, and the 5% depreciation in the quetzal against the dollar in the first half of January. However, thanks to a stringent monetary policy and some degree of recovery in the exchange rate, annual inflation estimated to have been 4% in 2000. The downturn in construction (-12%) and the slowdown in manufacturing activity (2.3%) had an adverse effect on formal employment. Moreover, a 10% rise in the minimum wage was approved in February, and an agreement was reached on the adoption of a scheme in the private sector for tying wage increases to productivity.

As in 1999, the balance of payments current account showed a deficit of over 5% of GDP. By contrast, there was a substantial inflow of short-term capital, including repatriation of funds by residents, which brought the international reserve balance to US$ 1.8 billion, an increase of 50%.

A fall in coffee prices resulted in a decline in export earnings from this commodity despite a bumper crop. Sugar exports fell in both value and volume. On the other hand, non-traditional exports strengthened by 19.1%. Maquila exports expanded by 22.4%, despite the lack of new investments. Fuel imports increased by close to 50%. With respect to other imports, intermediate goods were up by 12%, and machinery, by 5.8%, while imports of consumer goods fell. The external public debt was reduced by 2% compared with 1999, and the debt servicing payment was equivalent to 4.7% of exports, a lower percentage than in 1999 (6.9%).

Honduras

The Honduran economy staged a strong reactivation, with GDP growing by close to 4% after having declined the year before. Per capita GDP increased by around 1%. The upturn in activity was led by the agricultural export and manufacturing sectors. In view of the economic significance of these activities, employment in the agricultural, manufacturing and maquila sectors was expected to improve somewhat upon its 1999 levels.

Economic policy was directed towards keeping major macroeconomic variables in balance, promoting the recovery and implementing the poverty reduction strategy that was required in order for Honduras to qualify for the Heavily Indebted Poor Countries (HIPC) debt relief initiative.

At 10.6%, inflation was close to its 1999 level. The fiscal deficit was equivalent to 4% of GDP and was financed mainly through loans and grants from abroad, which, by enabling the central government to avoid using domestic credit, reduced the inflationary impact of the deficit.

Tax revenues grew at a slightly slower rate than inflation. If non-tax income (11% of all public-sector revenues) is included, the central government recorded total income equivalent to almost 18% of GDP (1.5 percentage points less than in 1999). Total government expenditure declined slightly (from 22.5% to 21.9%). The most significant component was capital expenditure, much of which was associated with reconstruction work and the poverty reduction strategy called for in the country's 1999 agreement with the International Monetary Fund (IMF) (revised in early 2000). The reconstruction work carried out since Hurricane Mitch has proceeded more slowly than planned owing to implementation-related problems.

In view of the relatively abundant inflow of foreign exchange, the lempira tended to strengthen, and its annual rate of depreciation was approximately 5%.

As anticipated, the average tariff on final consumer goods remained fixed at 15% from January on. The northern triangle countries (El Salvador, Guatemala and Honduras) signed a free trade agreement with Mexico. The text was awaiting ratification by the respective congresses and was to enter into force in January 2001. The agreement negotiated with Chile in 1999 has been placed on hold, pending definition of tax reductions for sensitive products and details relating to rules of origin. Negotiations have been initiated or are being pursued with Panama, Colombia and the Andean Community, as well. Honduras has joined the customs union that was originally promoted by El Salvador and Guatemala.

Open-market operations have continued to serve as the authorities' main monetary policy instrument. By year's end government issues outstanding were almost double the December 1999 figure.

The annual variation in the broad money supply was 12.4%, the lowest in six years and scarcely more than half the rate recorded in 1999. The momentum behind net domestic borrowing came almost entirely from the use of public-sector resources to cover reconstruction expenses. Bank credit to the private sector is estimated to have increased by close to 10%, which is equivalent to a slight decline in real terms.

Lending rates trended downward but were still high, and spreads remained wide. Bank supervision was also strengthened and, as a result, an improvement was seen in bank capitalization and compliance with legal reserve requirements.

HONDURAS: MAIN ECONOMIC INDICATORS

	1998	1999	2000[a]
	Annual growth rates		
Gross domestic product	2.9	-1.9	4.0
Consumer prices	15.6	10.9	10.6
Money (M1)	12.7	21.8	14.7
Real effective exchange rate [b]	-6.7	-3.1	-2.7
Terms of trade	2.3	-6.6	-5.8
	Percentages		
Urban unemployment rate	5.2	5.3	...
Fiscal balance/GDP	-1.1	-2.9	-4.0
Real deposit rate	4.5	6.9	4.7
Real lending rate	15.0	16.6	14.6
	Millions of dollars		
Exports of goods and services	2 476	2 312	2 625
Imports of goods and services	2 797	3 056	3 465
Current account	-42	-176	-430
Capital and financial account	184	474	270
Overall balance	142	297	-160

Source: Statistical Appendix.
[a] Preliminary estimates.
[b] A negative rate indicates an appreciation of the currency in real terms.

In December 1999, Honduras applied for the Heavily Indebted Poor Countries (HIPC) debt relief initiative. In June 2000, IMF and the World Bank determined that the country was eligible for the initiative, which is expected to provide US$ 556 million in external debt relief at net present value, which is equivalent to close to 14% of the balance at year-end (estimated at approximately US$ 4 billion). Two fifths of the reduction will be provided by bilateral creditors and the rest by multilateral agencies. The agreement includes an interim debt relief arrangement funded by IMF, the World Bank and the Inter-American Development Bank. The HIPC initiative requires Honduras to comply with a broad range of macroeconomic, social and institutional conditions.

Competitive bidding for the telecommunications firm, Hondutel, was declared void and privatization of the company was once again postponed, which will make it necessary to redesign the process. The agreement with IMF called for privatization of energy distribution, but the adoption of a framework law for the electrical power sector remains pending. As planned, operating concessions for the country's four international airports were awarded.

Domestic demand reacted moderately to higher consumer spending, which was fuelled by a wage increase in the early part of the year and, in subsequent months, by investment.

Agriculture was the fastest-growing sector and nearly doubled the overall GDP growth rate. This improvement is largely attributable to an upturn in export crops (bananas, coffee and African palm).

Manufactures also performed well. In both this sector and agriculture, however, financing problems continue to limit both the rate and the scale of the recovery. Transport, services and commerce all expanded, but the construction industry grew more slowly than expected. *Maquila* operations also continued to strengthen.

Inflation was in the double digits as a result of the rise in fuel prices, the increase in electricity rates and the effect of the 8% minimum wage hike.

The balance-of-payments current account deficit stood at US$ 430 million, which represented an increase from 3.2% of GDP in 1999 to 7.2% in 2000. The imbalance was attributable to the country's US$ 840 million trade deficit.

Merchandise exports were up by almost 20%. This improvement was based on the recovery of banana-producing zones, whose export volumes were two and one half times their 1999 level (although still 40% lower than in 1998) and to a more plentiful coffee harvest, which made up for the erosion of prices on the international market. Exports from the *maquila* industry expanded by 20%. Merchandise imports were 12% higher.

The current account deficit was offset by remittances from Honduran nationals residing in the United States (estimated at some US$ 450 million) and direct investment flows (US$ 170 million). The net balance of international reserves is estimated at US$ 1.5 billion, or the equivalent of five months' worth of imports.

Mexico

The Mexican economy grew by 7%, thus outdistancing the target figure (4.5%) and the expectations formed early in the year (3.5%). Exports were buoyed by the United States economy and oil sales; imports matched their growth rate thanks to the strength of domestic demand and despite an increasingly restrictive monetary policy and tight bank credit. Rebounding real wages and rising employment drove up consumption by 8% and fixed investment by 11%.

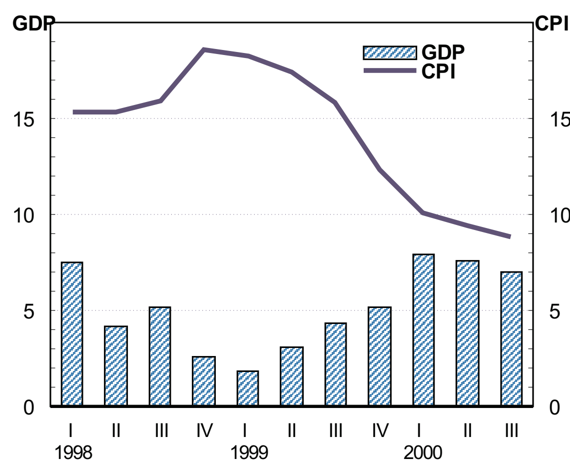
The real appreciation of the peso helped to bring inflation down to 8.9%. High oil prices generated a surplus that bolstered the economy and paved the way for the achievement of the target figure for the fiscal deficit (1% of GDP). FDI continued to flow into the country and helped to cover the deficit on the current account of the balance of payments (3% of GDP). The banking system remained depressed, as it continued to be affected by the fallout from the 1994-1995 banking crisis.

In 2001, the economy's growth rate is expected to slow to around 4.5%.

Economic policy focused on reducing inflation and keeping the external sector free from disequilibria, and this orientation took the form of tight monetary and fiscal policy measures. The financial armor put together in 1999 was reinforced by expanding the country's line of credit with international financial agencies and extending the North American framework agreement to December 2001, thus boosting the total from US$ 23.7 billion to US$ 26.44 billion.

Fiscal discipline and larger-than-expected inflows made it easier to finance public expenditure, which rose by 13.6% between January and September and was concentrated in education, health and social security (62%). Driven by the 28% jump in oil revenues, total public-sector income climbed by 15% to 35% of the total.

MEXICO: GROSS DOMESTIC PRODUCT AND INFLATION
(Percentage variation)



Source: ECLAC, on the basis of official figures.

The net external public debt shrank by nearly US$ 10 billion, falling to US$ 73.4 billion, or 12.5% of GDP (as compared to 13% of GDP in the case of the private-sector debt). Part of the reduction in the public debt was made possible by the retirement of US$ 6 billion in Brady bonds, which enabled the country to

pre-pay external obligations and thus realize savings in debt-servicing costs; US$ 3 billion in debts owed to the International Monetary Fund were also paid off early.

The peso appreciated in real terms, as oil sales and abundant FDI inflows generated a plentiful supply of foreign exchange, as well as helping to build up international reserves. As an annual average, the peso was worth 7% more in real terms than it was in 1999 and 15% more than in 1998. This means that the Mexican peso's real value in 2000 was more or less the same as it had been before the 1994 currency crisis.

Monetary policy was tightened as the year progressed in order to contain inflationary pressures and prevent the economy from overheating. As a result of this policy stance, real interest rates on loans remained high, which did nothing to buttress the recovery of lending activity; net commercial bank credit to the private sector thus declined for the sixth year running in real terms, falling to just one fourth its 1994 level. The sluggishness of domestic financing for production was partly offset by non-bank mechanisms such as supplier credit and foreign loans.

Primarily through medium- and long-term issues, the public domestic debt rose to 11% of GDP. The liabilities of the Bank Savings Protection Institute (IPAB) were reduced to 14% of GDP as part of the strategy of using budget transfers, the proceeds from the sale of assets and bank dues to cover the real debt service. Taken together, the domestic debt and IPAB liabilities amounted to 25% of GDP.

Although economic activity slowed as the year wore on, GDP growth was the highest in 19 years (comparable to the 1997 rate), with transport and communications, commerce and restaurants, and manufacturing exhibiting particular buoyancy. The investment-output ratio climbed to over 20% and the domestic savings rate reached 21.7% of GDP, which was seven points higher than the 1994 figure.

The recovery of real wages, higher employment and non-bank credit mechanisms (mainly for the purchase of consumer durables) all contributed to a strong upturn in private spending. Retail sales were up by 10% in real terms and sales of motor vehicles had climbed by 33% as of October.

The primary sector picked up its pace of activity, and particularly strong showings were turned in by producers of wheat, rice, soybeans, tomatoes, sesame, beans, lemons and marine products. The manufacturing sector posted an average growth rate of over 7%, but trends in the various activities within the sector remained extremely uneven, since the smaller firms suffer from chronic shortcomings. The fastest-growing activities were metal products, machinery and equipment. The automotive industry's total output amounted to 1.6 million units for the period January-October (28% more than in the same period of 1999); the production of vehicles for export was especially dynamic, rising by 35% to account for over three fourths of total production.

The number of persons employed in the formal sector exceeded 15 million (6% more than in 1999); in the *maquila* industry, a 14% increase in employment brought the total number of employees up to 1.3 million (30% of total manufacturing employment). Meanwhile, open unemployment crept towards the 2% mark. Underemployment was high, however, and this was reflected in the expansion of the informal economy, which provides 29% of all jobs in the country.

The increase in consumer prices (8.9%) was lower than the official target (10%). International

MEXICO: MAIN ECONOMIC INDICATORS

	1998	1999	2000[a]
	Annual growth rates		
Gross domestic product	4.9	3.7	7.0
Consumer prices	18.6	12.3	8.9
Real wages	2.8	0.9	6.1
Money (M1)	16.2	28.5	21.0
Real effective exchange rate [b]	3.3	-8.4	-7.0
Terms of trade	-3.5	1.9	2.5
	Percentages		
Urban unemployment rate	3.2	2.5	2.3
Fiscal balance/GDP	-1.2	-1.1	-1.0
Real deposit rate	4.5	2.6	3.6
Real lending rate	11.1	7.9	7.6
	Millions of dollars		
Exports of goods and services	129 387	148 601	182 275
Imports of goods and services	137 859	155 581	193 550
Current account	-15 726	-14 013	-18 960
Capital and financial account	18 936	18 290	20 760
Overall balance	3 210	4 277	1 800

Source: Statistical Appendix.
[a] Preliminary estimates.
[b] A negative rate indicates an appreciation of the currency in real terms.

hydrocarbons prices did not carry over to domestic gasoline prices because of the policy of instituting gradual, pre-announced increases. In contrast, the price of natural gas (which is determined by international prices) nearly doubled, thereby impacting a number of industries.

In the second half of the year, there were signs that the downward trend in inflation could be bottoming out. Contractual wage hikes outstripped expectations; the increase in real wages was greater than the gain in labour productivity; aggregate demand grew faster than supply; and government-administered prices outpaced the targeted rate of inflation.

In October the Banco de México announced that the inflation target for the coming year would be 6.5% and proposed that this figure should be used as a benchmark for wage negotiations. Economic agents felt that it was unlikely that this target would be achieved, however, and contractual wage increases were set at around 11% instead. This suggests that inflation in 2001 may exceed the Banco de México target figure, but it would not prevent a further rebound in real wages, which were raised by 6% in the manufacturing sector and 7% in commerce.

The balance-of-payments current account ran a deficit of almost US$ 19 billion (35% more than in 1999) which was covered primarily by long-term private-sector resources. This shortfall was the net outcome of a combination of deficits on the trade and services accounts and a surplus on the transfers account.

The merchandise trade deficit was around US$ 8.2 billion (a 50% increase over the 1999 figure). The non-oil trade deficit is estimated to be about US$ 20 billion, versus a negative balance of US$ 12 billion in 1999. Total (goods and services) trade represented nearly two thirds of GDP.

Exports and imports grew at nearly the same rate (24%). Oil sales almost doubled due to the increase in prices (62%), since the volume of shipments rose by just 5%. Exports of manufactures climbed 20% and represented 87% of the total. Within this category, *maquila* exports jumped by 26% (47% of the total).

The expansion of domestic demand contributed to the 40% increase in imports of consumer goods (versus 9.6% in 1999), although these products represented a scant 9% of total imports. Imports of intermediate goods were up by 24% and continued to account for the largest share of the total. The United States was the country's main trading partner.

Foreign investment shrank from US$ 22.75 billion to under US$ 20 billion; this decrease was attributable to the decline in inbound portfolio investment, since direct investment amounted to an all-time record of US$ 13 billion. The end result was a US$ 21 billion surplus on the capital and financial account.

The free trade agreement with the European Union entered into force, and similar accords were signed with the Northern Triangle countries (El Salvador, Guatemala and Honduras) and the European Free Trade Association (EFTA) that will enter into effect in 2001.

Nicaragua

GDP grew by 5.5%, which was lower than the 1999 figure. Domestic demand contracted because private investment shrank in response to tight credit and high financial costs. The uncertainty typically observed during an election year was also a factor, as were the fiscal and monetary stabilization policies implemented early in the year. Domestic demand would have receded even further had it not been for the increase in public-sector consumption and the continuing high level of public investment. The country's financial system experienced solvency problems that led banks to raise their interest rates, and this had an impact on business activity.

Public accounts worsened and inflation climbed at a fairly moderate pace to 9.2%. The currency's rate of devaluation held steady, and this translated into an appreciation of the córdoba in real terms. Open unemployment shrank to 9% and the external sector's current account deficit was reduced by 10%, which helped the country to build up its net international reserves.

No headway was made in reducing the external debt –even though the country had been declared eligible for the Heavily Indebted Poor Countries (HIPC) debt relief initiative a year ago– owing to the existence of macroeconomic disequilibria that made it necessary to revise the targets agreed upon with the International Monetary Fund.

Progress was made, on the other hand, in the implementation of structural reforms, especially legislative or regulatory provisions for dealing with the pension system, social security, customs administration and the promotion of foreign investment. The two distributors for Enel, the country's electricity company, were sold, but the authorities were unable to transfer ownership of the generating companies, and the privatization of the telephone company, Enitel, fell behind schedule.

Despite corrective measures and improved management, the central government's deficit (after grants and donations) rose from 4.5% of GDP in 1999 to 5.5% in 2000. This increase was attributable to higher expenditure on the reconstruction of roads and bridges washed away by heavy rains in the third quarter of 1999 and to the cost of introducing pension system reforms, holding municipal elections and implementing constitutional reforms that increased the size of the Supreme Court, the Supreme Electoral Council and the Office of the Comptroller-General.

The excise tax on goods produced by State-run industries was raised again, and rate hikes for basic utilities were adjusted.

The central bank made net placements of negotiable certificates of investment (CENIs) and foreign-exchange bonds (BOMEX bonds). These issues, together with higher reserve requirements, counteracted those factors that tended to bring about an increase in net domestic assets. These measures and foreign-exchange earnings from privatization operations reinforced the country's international reserves.

The year-on-year growth of monetary aggregates slowed. At the same time, net domestic credit expanded, mainly due to the combined effect of the withdrawal of deposits from the non-financial public sector's accounts with the central bank and the opening of a special line of credit which, upon the closure of the Banco Popular, permitted that bank's customers to withdraw their funds.

Inflationary pressure made it impossible for the authorities to continue with the reduction in the córdoba's rate of depreciation, and the real effective exchange rate consequently declined slightly.

Duties on imports of powdered milk, polished and unpolished rice, sorghum and yellow corn were raised above the ceiling rate (10%). At the same time, a guaranteed domestic floor price was established for soybean producers. In addition, the sector's tariff exemptions for imports of inputs and of intermediate and capital goods were extended up to December 2002.

Nicaragua joined with El Salvador and Guatemala in signing a tri-national declaration calling for the establishment of a regional system for ensuring economic and social justice and well-being, the formation of a customs union, the consolidation of the financial system, the strengthening of the Central American subregion and sustainable development. The creation of an interoceanic intermodal shipping corridor is also planned.

The public sector's total outstanding external debt is estimated at US$ 6.65 billion, which is around US$ 150 million more than the year before. In order to cover its external borrowing requirements, the government has relied primarily on loans that are extended on highly concessional terms.

On the supply side, the country's economic growth was based on the sustained pace of reconstruction work and the recovery of farm production, together with these activities' spillover effects on manufacturing, commerce and transport. On the demand side, the main contributing factors were public expenditure (on consumption and, to a lesser degree, investment) and rebounding exports, especially of traditional products.

Although the construction industry has remained buoyant, its pace of activity has gradually been declining because government allocations for the special reconstruction programme launched in the wake of Hurricane Mitch in 1998 are being scaled back and because private investment in non-residential construction is decreasing as a number of major hotel projects have reached their final stages.

Inflation is estimated to have reached 9.2%, or two percentage points more than in 1999. Higher utility rates, shipping charges, and prices for petroleum products and building materials were part of the reason for this rise.

Despite some wage hikes in the public sector and higher wage levels in a number of economic sectors, average real wages remained virtually constant. The country's economic growth is thought to have brought about a reduction in unemployment from 10.7% to 9%, but underemployment climbed once again.

The current account deficit was cut to US$ 990 million thanks to a smaller trade deficit and a higher level of unrequited private transfers from abroad. The deficits on the services and income accounts were, for all intents and purposes, unchanged. Despite the decreases posted on the capital and financial account, at year's end it appears that the overall balance of payments generated a surplus and that the country managed to consolidate its net international reserves position.

The merchandise trade deficit (42% of GDP) narrowed by 7.5% as the value of imports held more or less steady and exports rebounded. Total exports of goods, including net exports of firms operating in the free zone, amounted to US$ 690 million. This increase was led by higher sales of traditional products (coffee, sugar, bananas, lobster and shrimp) as well as of some non-traditional exports (including peanuts, cheese and cattle).

The higher value of imports of oil, fuels and lubricants played an important role in shaping the trend in the value of imports, since, owing to the slowdown in economic activity, imports of other raw materials and capital goods were sharply lower and imports of consumer goods were virtually flat.

NICARAGUA: MAIN ECONOMIC INDICATORS

	1998	1999	2000[a]
	Annual growth rates		
Gross domestic product	4.1	7.0	5.5
Consumer prices	18.5	7.2	9.2
Real wages	7.4	4.3	1.6
Money (M1)	17.1	20.7	16.0
Real effective exchange rate [b]	0.7	1.0	-1.9
Terms of trade	4.2	-7.2	-3.8
	Percentages		
Unemployment rate	13.2	10.7	9.0
Fiscal balance/GDP	-1.8	-4.5	-5.5
Real deposit rate	-1.9	-0.9	-2.4
Real lending rate	7.8	9.8	8.3
	Millions of dollars		
Exports of goods and services	830	840	925
Imports of goods and services	1 658	2 028	2 030
Current account	-813	-1 086	-990
Capital and financial account	583	995	1 000
Overall balance	-230	-91	10

Source: Statistical Appendix.
[a] Preliminary estimates.
[b] A negative rate indicates an appreciation of the currency in real terms.

Panama

For the third consecutive year, there was a slowdown in the Panamanian economy, with GDP growth coming to just 2.5%. The contraction in capital formation that followed the completion of large-scale infrastructure works and slackening consumption reduced domestic demand. External demand increased moderately, mainly as a result of an upsurge in sales in the Colón Free Zone, which had declined in the two previous years. Unemployment tended to rise, and the minimum wage was raised by 10% in August. Although the rise in international fuel prices drove up wholesale prices, consumer price inflation was less strongly affected. Cutbacks in public investment expenditure helped to reduce the fiscal deficit, and measures were taken to curb the country's large deficit on the balance-of-payments current account.

The main focuses of macroeconomic policy were to strengthen the financial position of the public sector, reduce the foreign debt and rein in the country's large deficit on the balance-of-payments current account. In support of the government programme, a precautionary special drawing rights (SDRs) arrangement was signed midway through the year with the International Monetary Fund.

In the first nine months of the year, the public sector's operations yielded a surplus equivalent to 0.9% of GDP, thereby ensuring its achievement of the goal set with the Fund, despite the central government deficit. One of the factors that made this possible was the reduction in capital expenditure, particularly by the central government, since there was a slight increase in current expenditure. Central government revenues grew by 2.1% owing to an increase in non-tax income (mainly the contributions to the Treasury made by public-sector companies), as tax receipts were 3.4% lower because of a reduction in indirect taxes.

The public-sector debt remained practically unchanged, with outstanding external liabilities standing at US$ 5.445 billion. A US$ 350 million global bond was placed on international markets, and the proceeds were allocated to the public investment programme. In addition, significant repayments were made, including a buy-back of US$ 153.5 million in Brady bonds. The issue of Treasury bills made it possible to amortize a number of domestic debts.

At the close of the third quarter, the assets of the international banking centre had increased by 2.4%. This was the net outcome of a decrease in international credit operations (-7.6%) due to continuing problems with the centre's main Latin American clients, and an increase in domestic lending (6.9%), although its expansion was slower than in 1999.

On the domestic front, there was a slowdown in the high rate of expansion of personal consumer loans, while other types of credit maintained their rate of increase (residential construction, commerce, industry and the primary sector).

Interest rates on loans slipped back to the level reached in August 1999, after a short period of marginal increases. The policy of providing preferential credit for low-income housing remained in force following a decision taken in September 1999 to continue its implementation.

The country's largest privatization operations were carried out in previous years, and in 2000 no progress was made in the plans to transfer ownership of the public radio and television services, the international airport, the Atlapa Convention Centre or the water and sewerage utility, IDAAN. On another front, negotiations with Chile and Mexico on a trade and investment agreement

PANAMA: MAIN ECONOMIC INDICATORS

	1998	1999	2000[a]
	Annual growth rates		
Gross domestic product	4.4	3.0	2.5
Consumer prices	1.4	1.5	1.4
Terms of trade	-0.1	2.5	-5.7
	Percentages		
Urban unemployment rate	15.2	14.0	15.2
Fiscal balance/GDP	-5.4	-2.3	-2.4
	Millions of dollars		
Exports of goods and services	8 078	7 015	7 510
Imports of goods and services	8 857	7 814	8 340
Current account	-1 175	-1 376	-1 240
Capital and financial account	712	1 228	840
Overall balance	-463	-148	-400

Source: Statistical Appendix.
[a] Preliminary estimates.

did not prosper, but talks with the Central American countries on market access for goods, trade in services and investment continued.

Although there was an upturn in activity within the Colón Free Zone –after two years of declining activity that had triggered a 22% drop in re-exports– the momentum of international services waned, particularly in banking. The main areas of activity serving the domestic market turned in a very uneven performance, but the general trend was downward. In the third quarter, however, there were signs of a reactivation.

The net cargo shipped through the Panama Canal rose by 2.4% and toll receipts increased by 2.6% in the first nine months of the year. The moderate expansion of port services marked a contrast with the growth rate recorded for 1999.

The construction industry's growth rate slowed to 2% following a 16% increase in 1999. The agricultural sector grew by a scant 0.7% after having declined by a slight amount in 1999; the improvement was the result of the combined effects of rebounding banana production and a smaller basic grain harvest owing to the drought, which had a particularly severe effect on the rice crop.

With domestic demand weakening, domestic commerce slumped by 5.8%. For the second year in a row, manufacturing production contracted by about 5% as the sector continued to adjust to the new conditions created by of trade liberalization.

Consumer prices climbed by about 1.5%. Wholesale prices were up by 9% owing to the frequent adjustments made in fuel prices in line with international price trends. These adjustments made it possible to maintain the traditional differential between the two indices.

Owing to the decrease in production activity, especially in the wake of the downturn in investment, the unemployment rate for the metropolitan region increased from 14% to 15.2% between August 1999 and August 2000.

The current account deficit amounted to US$ 1.24 billion, a figure equivalent to 12% of GDP and slightly less than the US$ 1.376 billion recorded in 1999. This was mainly due to the results for merchandise trade, as services continued to show a significant surplus. Financing for the current account came mainly from FDI inflows amounting to about US$ 400 million.

Exports of goods, which grew by 6.7% in terms of value to US$ 5.665 billion, were led by the recovery of re-exports from the Colón Free Zone. Exports of domestically-produced goods, which represent 13% of the total, climbed by 6% thanks to higher sales of products such as flour and fish oil, shrimp larvae, coffee and sugar. On the other hand, sales of bananas, shrimp, cattle and petroleum products fell.

Imports of goods were up by 6.3%, particularly because of the 11.3% increase in purchases by the Colón Free Zone. National imports, representing one half of the total, were virtually flat, even though oil imports increased by 53%. There were significant reductions in imports of capital goods (–8%) and of transport and communications equipment (10%).

The services account posted a surplus on the order of US$ 650 million. This result was associated with Panama Canal operations and a 23% increase in earnings from tourism.