Dominican Republic

At the end of 2006, the economy of the Dominican Republic had chalked up five consecutive quarters of growth in double digits. For the year as a whole, overall growth is estimated at 10%. Investment spending has now replaced consumption as the driving force behind such growth. Another particular characteristic is that the expansion has occurred mainly on the back of goods production activities, and to a lesser extent on the strength of service sectors. Despite higher international oil prices, inflation is expected to fall to 4.5%. In 2007, economic growth is predicted to be more subdued, at around 7%. Also, the fiscal reform being debated in Congress is expected to increase the government's tax revenue by about 1.5% of GDP for the following year.

Public spending policy was clearly expansionary. In an electoral year, one of the most buoyant components was current expenditure. Subsidies to the energy sector (electricity and liquefied petroleum gas) resulted in larger transfers, which represented the equivalent of almost 1% of GDP. At the same time, capital expenditure and the payment of financial liabilities rocketed during the year. At the end of the third quarter, central government investment was 71% higher than the year-earlier period, and amounted to almost 7% of GDP. Spending on public works, mainly channelled into the construction of the metro in Santo Domingo, was the determining factor behind the above-mentioned expansion. In the same period, external debt-servicing rose sharply: by 66% for interest payments and 158% for capital payments.

Fiscal revenues, on the other hand, were lower than expected. Despite the increase in selective consumption taxes (on beer and cigarettes), tax revenues did not generate the projected amount of resources. Furthermore, the anticipated elimination of the import tax (known as "banking commission") planned under the Dominican Republic-Central America-United States Free Trade Agreement, meant that, up to October, income from that source was 64% lower than in the year-earlier period. This source's contribution to tax revenues therefore fell from 12.4% to 3.9%. Despite growth in total central government income, the fiscal target of an overall surplus of 300 million Dominican pesos set at the beginning of the year will thus not be reached in 2006. A central government deficit equivalent to 1% of GDP is expected.

In 2006, the central bank maintained its strategy of controlling inflation. This strategy made it possible to achieve an inflation rate below the 6% to 8% band fixed in the agreement concluded with the International Monetary Fund early in the year and set out in the monetary programme. Open-market operations remained the main instrument of monetary policy. The policy of issuing certificates was in keeping with the economy's liquidity requirements and satisfied the demand for money arising from economic performance.

The increase in the central bank's balance of certificates did not involve any rises in interest payments. The lower financial cost of outstanding securities, resulting from successive reductions in their interest rates, facilitated a fresh decrease in the quasi-fiscal deficit from 3% of GDP at the end of 2005 to 2.6% by late 2006.

Achieving economic targets contributed to maintaining a stable foreign-exchange market. Above and beyond variations in the demand for foreign exchange (especially towards the end of the third quarter), the exchange rate remained fairly stable, which promoted higher capital inflows to the economy. In nominal terms, in October the Dominican peso experienced a 1.4% depreciation against the United States dollar compared with December 2005, while in real terms a slight appreciation of 0.1% was observed.

Growth in productive activity was buoyant throughout the year, with the growth rate stepping up in the second quarter. The main activities that contributed to aggregate GDP growth were the manufacturing, agricultural and

construction sectors, both in terms of their high rate of activity and their large share in total GDP. Commerce and communications also made a significant contribution to the overall growth rate.

Production in free zones declined once more in 2006, as the aggregate value of textiles shrank again. Petroleum refining showed an upturn in the third quarter, after posting negative growth up to June.

Cumulative inflation between January and September stood at 3.5%, which means it should close the year at around 4.5%. The general growth rate of domestic prices was determined by the impact of international oil prices. Without that factor, inflation would be 2.7% for the whole of 2006. This demonstrates the low level of growth of domestic prices.

The rise in output had an effect on the labour market. The open unemployment rate fell for the first time in three years, to come in at half a percentage point lower than in 2005. The weighted average of nominal minimum wages in the public and private sectors remained at the same levels as in 2005, when the nominal increase was about 30%.

At the end of the third quarter, the balance-of-payments current account posted a deficit of 1.6% of GDP, which is consistent with greater demand for imported goods in the light of the higher economic growth rate.

During the first nine months of the year, merchandise exports showed slow growth due to the fall of just under 6% in the value of exports from free zones (which make up 70% of the total). Non-maquila exports, on the other hand, soared (35.4%, mainly thanks to higher volumes and prices for exports of ferronickel). Growth in imports was entirely attributable to demand from the non-maquila sector of the economy. The most buoyant import goods in 2006 were raw materials, whose cumulative value up to September was 25% higher than the previous year. This is substantially different from 2005, when consumer goods were the fastest growing sector of merchandise imports. In the first three quarters of 2006, the oil bill was 25% higher than the year-earlier period, and represented 11.7% of total imports (compared with 10.7% in 2005).

Thanks to family remittances, net current transfers maintained their upward trend, and up to September amounted to 13% more than in the same period the previous year. At the same time, the balance-of-payments capital and financial account posted a positive balance, which was mainly due to the significant rise in foreign direct investment (18.8%), which was mainly channelled into the tourism sector and new projects in free zones.

At the end of the third quarter, international reserves had swelled significantly. By then, net available resources (US$ 959 million) were 28% higher than the minimum agreed with IMF for the entire year. In September, gross international reserves amounted to US$ 1.988 billion.

Table 1

DOMINICAN REPUBLIC: MAIN ECONOMIC INDICATORS

	2004	2005	2006 [a]
	Annual growth rates		
Gross domestic product	2.7	9.2	10.0
Consumer prices	28.7	7.4	5.2 [b]
Real minimum wage	-15.0	18.7	-7.0
Money (M1)	46.5	10.1	15.8 [c]
Terms of trade	-1.2	-1.0	-1.0
	Annual average percentages		
Urban unemployment rate [d]	18.4	18.0	16.4 [e]
Central government overall balance/GDP	-4.0	-0.7	-1.0
Nominal deposit rate	21.1	12.7	10.3 [f]
Nominal lending rate	30.3	21.4	16.3 [f]
	Millions of dollars		
Exports of goods and services	9 440	10 056	10 537
Imports of goods and services	9 101	11 333	12 393
Current account	1 047	-500	-807
Capital and financial account	-868	1 205	957
Overall balance	179	705	150

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

[a] Preliminary estimates.

[b] Twelve-month variation to November 2006.

[c] Year-on-year average variation, January to November.

[d] Includes hidden unemployment.

[e] Data refer to April.

[f] Average from January to October, annualized.