I. ECONOMIC ENVIRONMENT

(1) MAJOR FEATURES OF THE ECONOMY

1. The Rwandese Republic is a landlocked Central African country with an area of 26,300 km^2. It borders on Burundi to the south, the Democratic Republic of the Congo to the west, Uganda to the north and Tanzania to the east. Its population, of which more than 90 per cent is rural, was estimated at 8.3 million in 2002. With 315 inhabitants per square km., it is the most densely populated country in Africa. Its demographic structure has evolved but little since the first population census was taken in 1978. In 2001, 45 per cent of the population was under 15 years of age, and 75 per cent under 30.

2. With a per capita GDP of US$220, Rwanda is among the least developed countries. Close to two thirds of its population live in absolute poverty.[1] The country is still suffering from the economic consequences of the 1994 genocide[2], in particular the lack of infrastructure in certain regions as a result of the destruction perpetrated during the war and the public expenditure involved in compensating the genocide victims and meeting the costs generated by the 107,000 or so persons in prison awaiting trial for crimes relating to the genocide. The economic costs of Rwanda's prolonged involvement in the 1998-2002 war in the Democratic Republic of the Congo (DRC), particularly the military expenditures, have further hindered its reconstruction and development efforts. Added to this is the HIV-AIDS pandemic, which has also contributed to lowering life expectancy to about 39 years.

3. Agriculture employs more than 90 per cent of the population and accounts for some 44 per cent of real GDP, as against approximately 10 per cent for manufacturing activities and 46 per cent for services (Table I.1). The mining sector's contribution is negligible, although Rwanda does have certain mineral resources, notably colombo-tantalite (coltan) - the mining and export of which increased sharply in 2001 - and to a lesser extent, wolframite and cassiterite. Methane reserves amounting to 70 billion cubic meters are thought to exist near Lake Kivu, but they have not yet been exploited.[3] Rwanda's agricultural activities consist chiefly of subsistence farming. Its high population density has led to soil depletion and reduced output due to continuous exploitation and the limited use of inputs. The weakness of its land tenure system has also contributed to this situation. Coffee and tea are the main cash crops. Together with coltan, they account for close to 95 per cent of goods exports. The low level of foreign investment, partly due to insecurity in the region, does not favour diversification of the country's production and export structure. This lack of diversification has left Rwanda vulnerable to external shocks of a climatic nature or resulting from international market fluctuations.

4. The national currency, the Rwanda franc (RF), has a managed floating exchange rate with no pre-announced path.[4] Rwanda accepted Article VIII of the IMF Articles of Agreement in 1998. It has also liberalized certain capital account transactions. Indeed, any resident may open a foreign currency account in an authorized bank in Rwanda, while non-resident foreign currency accounts have been completely liberalized. Since 2000, residents have been able to withdraw freely up to US$50,000 per year, or the equivalent thereof in any other foreign currency, from their foreign currency accounts. Foreign currency can be freely transferred from abroad. There are no restrictions on foreign direct investment or on the repatriation of the net return on such investments and of income relating thereto, or of the proceeds from the transfer or disposal of capital. Residents may take out foreign currency

[1] i.e. on less than US$1 per day.
[2] Close to one million people were killed, while some 3 million went into exile in the neighbouring countries.
[3] See the website www.mbendi.co.za.
[4] IMF (2002).

loans from non-residents. Non-residents are free to buy treasury bills, subject to certain conditions (Chapter IV.2).

Table I.1
Main economic indicators, 1995-2002[a]

	1995	1996	1997	1998	1999	2000	2001	2002
				Percentage				
Miscellaneous								
Real GDP growth	35.2	12.7	13.8	8.9	7.6	6.0	6.7	*9.4*
Inflation rate (measured on the basis of consumer prices)[b]	..	7.4	12	6.2	9.8	4.3	2.9	2.5
Interest rate (end of period)								
- Borrowing rate	..	..	8.24	7.76	8.75	10.11	10.18	9.02
- Lending rate	..	..	16.2	17.1	16.8	17.0	17.29	16.4
Exchange rate								
Rwanda francs per US$ (end of period)	299.8	304.2	304.8	320.1	349.2	430.3	455.8	511.9
Nominal effective exchange rate (end of period – rate of change)[c]	-54.8	3.8	12.3	-11.9	5.7	-12.3	-3.4	-14.8
Real effective exchange rate (end of period – rate of change)[c]	-39.7	8.6	26.5	-18.2	5.1	-9.7	-5.3	-12.0
Share of real GDP								
Agriculture	44.0	46.8	42.8	43.4	43.9	45.1	*45.8*	..
Mining and quarrying industry	0.1	0.1	0.2	0.3	0.2	0.2	*0.2*	..
Manufacturing industry	10.2	10.5	11.0	10.5	9.4	8.5	*8.6*	..
Services	45.7	42.6	46.0	45.8	46.5	46.1	*45.4*	..
				Percentage of GDP				
National accounts								
Domestic final consumption	107.3	104.2	106.0	103.5	98.6	98.0	*95.5*	..
Government authorities	10.3	11.5	9.6	10.0	11.0	10.5	*11.7*	..
Households	96.9	92.7	96.4	93.5	87.6	87.5	*83.9*	..
Domestic investment	13.4	13.0	15.6	18.5	19.0	15.2	*14.7*	..
Public	8.1	8.4	9.3	8.5	7.0	5.2	*5.3*	..
Private	5.3	4.6	6.2	10.0	12.0	10.1	*9.4*	..
Exports of goods and non-factor services	5.2	6.5	7.4	7.0	7.7	7.9	*10.4*	..
Imports of goods and non-factor services	25.8	23.7	28.9	29.0	25.3	21.2	*20.6*	..
				Percentage of GDP				
Public finance[d]								
Deficit (-) or surplus (+)	1.6	-3.6	-2.2	-6.7	-6.4	-1.5	-5.3	-2.0
Deficit (-) or surplus (+), excluding grants	-13.7	-13.2	-9.2	-8.3	-9.7	-8.9	-9.5	-11.0
Overall revenue plus external grants	18.1	16.7	17.2	15.9	16.1	18.8	19.8	20.8
Expenditure plus loans minus refunds	11.3	7.4	6.8	5.3	5.9	9.1	8.4	8.6
Statistical discrepancies	20.5	22.5	19.6	18.9	21.8	19.4	21.0	23.2
				Annual growth rate				
Monetary situation (at 31 December)								
M1 (fiduciary money + scriptural money)	41.1	11.7	22.7	-0.8	7.0	1.6	5.8	..
M2 (M1 + demand deposits)	69.5	8.6	29.1	3.5	7.9	12.6	14.0	..
				Percentage of GDP				
External accounts								
Balance in the current transactions account	-3.1	-6.7	-9.5	-9.6	-7.6	-5.0	-5.9	-7.3
of which: trade balance	-11.1	-10.9	-10.0	-9.7	-9.8	-8.4	-8.5	-9.6
Capital account balance	7.2	6.5	6.3	4.8	3.7	4.1	3.9	3.8
Financial account balance	-1.5	1.7	2.4	2.6	3.4	1.8	4.6	4.3

.. Not available

a Figures in italics are estimates
b Annual average
c The sign (-) indicates depreciation
d At 31 December

Source: IMF (2003), *International Financial Statistics*, October; IMF (2003), *Country Report – Rwanda*, 29 May and *Statistical Appendix*, 5 July 2002; and National Bank of Rwanda, available at: httpt://www.bnr.rw/bnrnet/.

5. Rwanda's budget remains heavily dependent on foreign aid (US$45 per inhabitant, 18 per cent of the value of imports of goods and services, and 9.2 per cent of GDP in 1999). Rwanda is a heavily indebted poor country (HIPC), with an overall external debt of US$1.4 billion at the end of 2002.

Some 89 per cent of its debt is multilateral, its main multilateral creditor being the International Development Association. Close to 46 per cent of its bilateral debt comes from the Paris Club creditors, chiefly France. The other bilateral creditors include the People's Republic of China, Kuwait and Saudi Arabia. Rwanda qualified for debt relief under the HIPC initiative in December 2000, with a planned reduction at that date of 71 per cent of its current net value, i.e. US$810 million.

(2) RECENT ECONOMIC PERFORMANCE

6. Rwanda is pursuing its reconstruction programme, largely funded by foreign aid. Thanks to this programme, it has been able to bring its economy back to the level of 1990, with a real GDP for 2000 matching the 1990 figure. Despite a decline in the terms of trade of some 40 per cent between 2000 and 2002 (due to the fall in coffee and coltan prices), real GDP grew by 9.4 per cent in 2002 (as compared to 6 per cent in 2000 and 6.7 per cent in 2001), thanks in particular to the construction industry and agriculture. Estimated growth for 2003 is about 3.5 per cent.

7. The exchange rate system was partially liberalized in 1995, and payment restrictions on current transactions were abolished in 1998. Under Article 45 of the Exchange Regulations, export proceeds must be repatriated within three months from the date of physical departure of the goods. They must either be surrendered onto the exchange market or preserved in foreign currency in accounts opened in authorized banks. Should any unforeseen circumstances delay payment, the National Bank of Rwanda (NBR) must be so notified. The obligation to surrender foreign exchange was abolished in 1997, enabling exporters to use the totality of their export revenue for current transactions. However, the foreign currency repatriation obligation is still in force. A number of tariff reductions have been introduced (Chapter III(2)(iv)(b)). The privatization programme launched in 1997 has led to the privatization of more than 20 per cent of State enterprises (Chapter III(4)(iii)). Thanks to the pursuance by the NBR of a monetary policy aimed at controlling the growth of monetary aggregates[5] and the improvement of tax planning, including measures to boost public revenue, the inflation rate was brought back to under four per cent in the year 2000.

8. Public revenue has risen thanks, *inter alia*, to improved collection of customs revenue, the introduction of VAT in 2001 and the increase in its standard rate from 15 to 18 per cent, the introduction of excise duties on vehicles, the setting up of a tax auditing system for large enterprises to reduce tax evasion, and the subjection of all salary-related benefits and allowances to income tax. These measures led to an increase in public revenue from 9.7 per cent of GDP in 2002 to 11 per cent in 2003. A monthly expenditure control system and measures to reduce extra-budgetary expenditures have been introduced. However, the efficiency of these measures has been limited by the enormous cost of maintaining internal security and financing Rwanda's involvement in the DRC as well as expenses stemming from the national reconstruction and reconciliation process, malfunctions in the system of information (on loans) between the regional authorities and the central government, and substantial losses sustained during the transfer of budgeted funds between the central government and the regional authorities.[6] The public deficit (excluding grants) was at 8 to 10 per cent of GDP between 1998 and 2001, but increased in 2002 (11 per cent) and 2003 (12.1 per cent), owing mainly to non-recurrent expenses (estimated at 4.7 per cent of GDP in 2003) relating to the demobilization of

[5] The NBR fixes the levels of monetary aggregates and the inflation rate to be achieved, and uses, as its main monetary policy instruments, treasury bills, refinancing rates, and reserve requirement rates. The NBR, which does not have an independent committee for the formulation of monetary policy, is limited in its independence; the Chairman appoints the members of the NBR's Management Board. According to the Law on the Statutes of the NBR, the debit balance of the public treasury's current account during a particular financial year cannot exceed 11 per cent of the State's ordinary revenue in the course of the preceding financial year. Any expenditure beyond that limit is subject to parliamentary approval.

[6] Fofoack H., Obidgewu C., and Ngong R. (2003).

soldiers returning from the DRC, the holding of elections, the increase in strategic oil reserves, and the purchase of equipment for the health sector.

9. Excess expenditure at the end of 2002 and during the first half of 2003 was largely financed by the banking system. This led to a broad monetary growth rate (annualized) of 15 per cent in April 2003, as compared to the 8 per cent predicted for the entire year. These developments coincided with a sharp depreciation of the Rwanda franc (close to 45 per cent against the euro between April 2002 and April 2003), reflecting a sharp decline in export revenue as of the first quarter of 2002, and the appreciation of the euro. This acceleration of monetary growth coupled with the depreciation aggravated inflationary pressures. The annualized rate of inflation for April 2003 was 8 per cent (5 per cent excluding the impact of the demand for agricultural products) as against 3 per cent officially planned for that year and 2.5 per cent recorded in 2002, when a bumper harvest relieved inflationary pressures.

10. Faced with this situation, the NBR raised its refinancing rate to 14.5 per cent in 2003, while the weighted average treasury bills rate reached 11.5 per cent. In both cases these were the highest rates recorded since 1998.[7]

11. The pressure of fiscal policy on monetary policy is helping to maintain the interest rates applied by commercial banks at a high level (over 15 per cent) with an average spread between borrowing and lending rates fluctuating between 7 and 8 per cent. These high rates, which are also a reflection of the structural problems of the relatively under-developed banking system (Chapter IV (2)), constitute a major constraint on the financing of production.

(3) TRADE AND INVESTMENT

(i) Trade in goods and services

12. Goods exports accounted for 4 to 5 per cent of GDP between 1997 and 2002, while imports accounted for 12.5 to 14 per cent during the same period. Rwanda's balance of payments suffers from a chronic deficit, owing chiefly to the low coverage of goods imports by exports as well as to a high services account deficit (Table I.2). In spite of the steady fall in imports, the current account deficit has widened since 2001, reaching 7.3 per cent of GDP in 2002 and 11 per cent in 2003. This is due to a decline of close to 28 per cent in export revenue, caused by the fall in international prices and in the volume of Rwanda's main exports. However, official transfers and long-term loans have enabled Rwanda to maintain a slightly positive overall balance, and official gross reserves equivalent to approximately six months of imports in 2001 and 2002.

[7] The reserve requirement remained at 8 per cent.

Table I.2
Balance of payments, 1995-2002
(US$ million)

	1995	1996	1997	1998	1999	2000	2001	2002[a]
Current account balance	**-39.6**	**-93.1**	**-176.3**	**-190.2**	**-147.5**	**-90.2**	**-100.3**	**-127.4**
Trade balance	-143.7	-151.3	-184.5	-191.5	-186.7	-150.1	-144.4	-166.4
Exports, f.o.b..	50.4	62.0	93.0	64.1	62.0	89.8	93.5	67.3
Imports, f.o.b.	194.1	213.3	277.4	255.7	248.8	239.8	237.9	233.7
Services	-123.7	-127.8	-145.6	-159.1	-143.0	-141.4	-125.3	-136.7
Income	4.7	-14.1	-17.9	-6.6	-11.4	-15.4	-22.5	-19.1
Current transfers (net)	223.0	200.1	171.7	167.0	193.7	216.6	191.9	194.8
Capital account balance	**93.5**	**90.0**	**115.9**	**95.1**	**70.9**	**72.8**	**67.0**	**66.3**
Transfers	93.5	90.0	115.9	95.1	70.9	72.8	63.4	66.3
Debt forgiveness	0.0	0.0	0.0	0.0	0.0	0.0	3.6	0.0
Financial account balance	**-19.0**	**23.3**	**44.6**	**51.5**	**64.4**	**32.7**	**78.3**	**75.0**
Direct investment in Rwanda	2.0	2.2	2.6	7.1	1.7	8.1	3.8	2.6
Public sector capital	25.9	34.6	40.8	46.5	52.2	20.9	55.4	62.9
Other capital	-47.0	-13.6	1.2	-2.1	10.4	3.7	19.1	9.5
Errors and omissions	**16.4**	**-21.1**	**27.5**	**20.8**	**-5.0**	**-19.1**	**-20.5**	**5.3**
Overall balance	**51.2**	**-0.9**	**11.7**	**-22.8**	**-17.2**	**-3.8**	**24.4**	**19.3**
Financing	**-51.2**	**0.9**	**-11.7**	**22.8**	**17.2**	**3.8**	**-24.4**	**-19.3**
Change in net foreign assets of NBR	-46.7	-17.2	-29.2	3.8	10.1	-9.8	-25.1	-29.7
Change in arrears	-4.5	18.1	17.5	-58.2	-2.7	7.1	-37.8	4.6
Exceptional financing	0.0	0.0	0.0	77.2	9.7	6.4	38.6	5.9
Memorandum items:								
Gross official reserves[b]	3.3	2.7	4.0	4.6	4.7	5.4	5.8	6.3
External debt[c]	6.3	6.6	6.9	6.4	1.5	1.7	1.8	2.0
Overall balance (in percent of GDP)	4.0	-0.1	0.6	-1.1	-0.9	-0.2	1.4	1.1

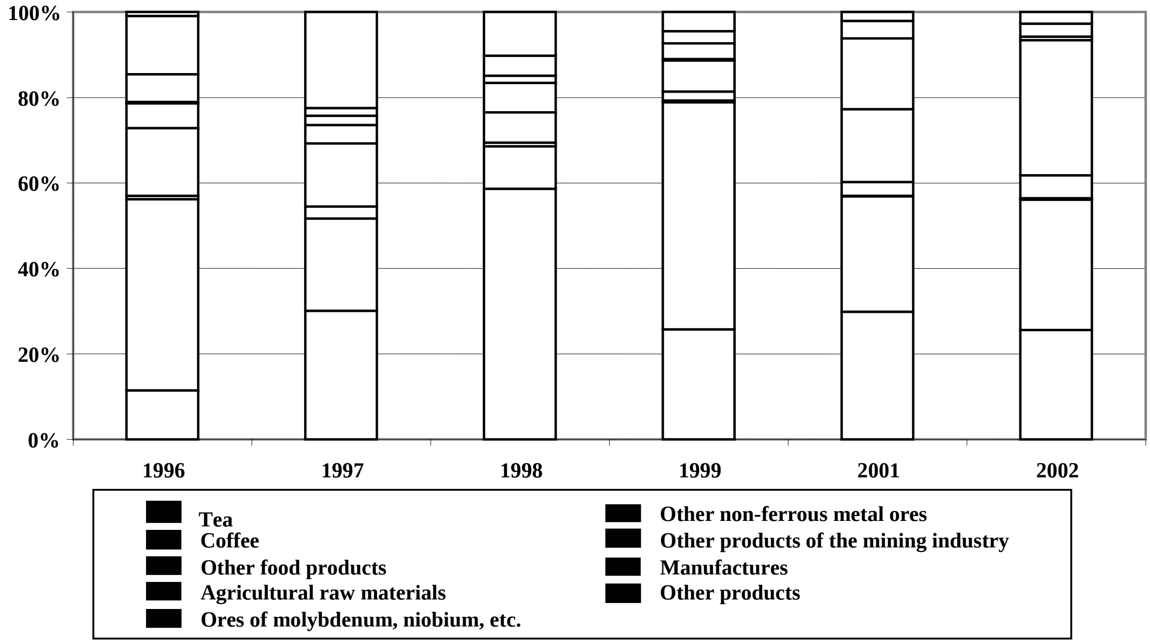
a Estimates.
b In months of imports of goods and services.
c In months of exports of goods and services.

Source: IMF (2003), *Country Report – Rwanda*, 29 May.

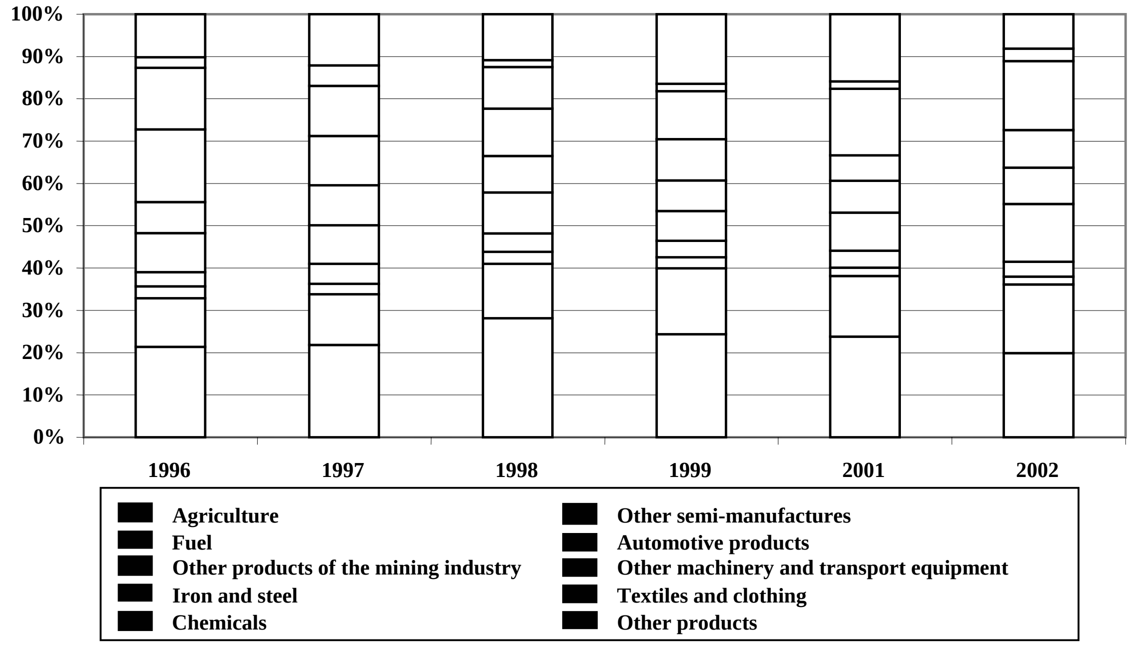
13. Rwanda exports chiefly agricultural products, in particular coffee and tea, to which it added coltan in 2001. These three products accounted for 92 per cent of its exports in 2001 and 77 per cent in 2002 (Chart I.1 and Table AI.2). Revenue from tea exports has remained more or less stable, while coltan export revenue fell by 65 per cent in 2002, *inter alia* owing to the 16 per cent decline in volume and to the fall in the world market price. The decline in revenue for 2003 was 48 per cent. Revenue from coffee exports fell by 13 per cent in 2002 and 14 per cent in 2003 owing to the fall in world prices, and to reduced output attributable to management problems, climatic conditions and an increase in the price of inputs. In spite of the Government's determination to diversify the structure of its exports, the share of manufactured goods has remained extremely low. A re-export trade, the extent of which varies from year to year, has also developed, with other African countries in particular. In 2002, re-exports accounted for around 16 per cent of Rwanda's overall exports. The main re-export products are fuel, worn clothing, "superwax" pagnes, and building materials, with the DRC and in particular the towns of Goma and Bukavu as the main destinations. These re-exports (or more precisely, transit activities) are stimulated by the reconstruction of Goma and by the insecurity involved in shipping goods to the DRC.

Chart I.1
Structure of trade in goods, 1996-2002

(a) Exports



(b) Imports



Source: WTO Secretariat calculations, based on data taken from Comtrade, UNSD (SITC, Rev.3).

14. The countries of Africa are the main destinations for Rwanda's exports, with Kenya alone accounting for some 55 per cent per annum on average during the period from 1996 to 2001 (Chart I.2). Tea is the main export to Kenya, while re-exports dominate trade with Tanzania and Uganda. After Africa, Europe is the second destination for Rwandan exports. The main European markets are Germany, Belgium, and since 2001, Switzerland (Table AI.4).

15. There was little evolution in the structure of Rwanda's imports between 1996 and 2001. They were dominated by manufactures, particularly machinery and transport equipment (Chart I.1 and Table AI.1). The increase in imports of consumer goods, telecommunications equipment and office machines reflects the economic recovery and, in particular, the expansion of service activities. The other main categories of imports into Rwanda are food products, both for final consumption and for use as inputs in agri-food production, and products of the mining and quarrying industry, in particular petroleum products.

16. Since 1998, the African countries, in particular Kenya, have constituted the main source of goods imported into Rwanda (Chart I.2). The share of the European countries, among which Belgium has a predominant position, decreased by about 9 percentage points between 1996 and 2001 (Table AI.3). The increase in the share of Asian countries (approximately 6 per cent) during the same period partly reflects the increase in the price of petroleum products, and to a lesser extent, the increase in the volume of manufactured goods imported from the People's Republic of China and Viet Nam.

17. Rwanda is a net services importer, with an average deficit (excluding factor income) of US$141 million per year between 1997 and 2001. Trade-related services imports grew rapidly between 1996 and 2001, in particular in the freight and transport category, where they increased by approximately 85 per cent, reflecting the economic recovery.

(ii) Investment

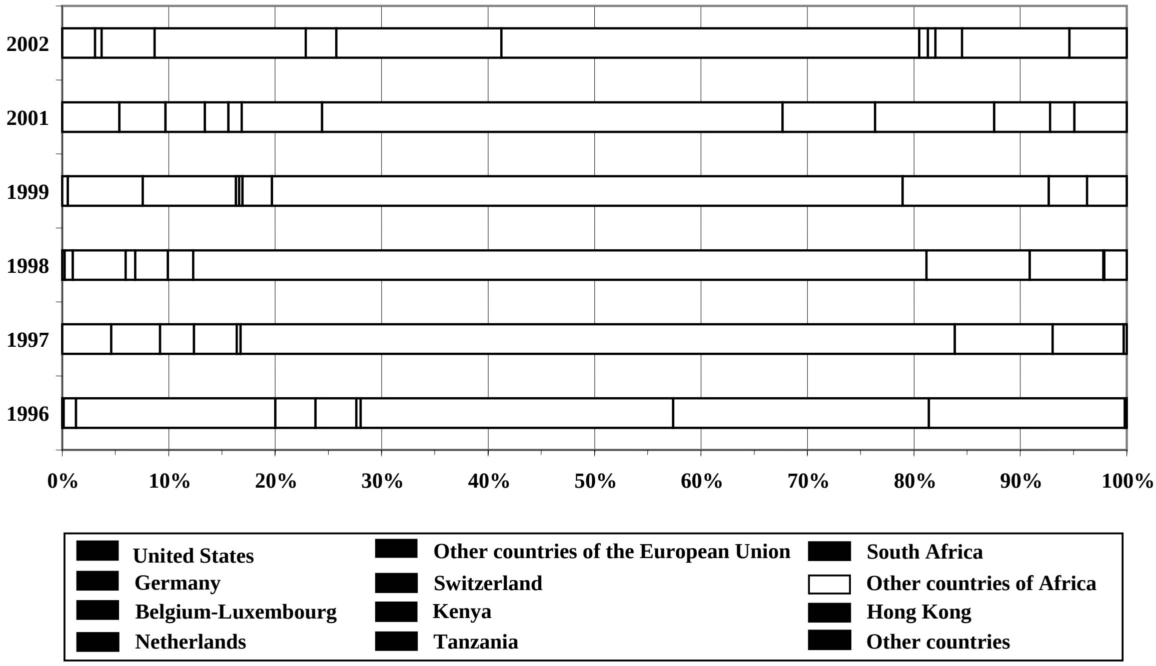
18. Foreign direct investment (FDI) flows reached RF 186.1 billion in 2001, 4.5 billion in 2002 and 9.7 billion in 2003.[8] This represents a considerable progression with respect to the average of US$3.1 billion for the period 1995 to 1999[9], and is undoubtedly the result of the economic performances relating to the reforms, including liberalization and privatization. Some 40 per cent of these investments in 2001, and 20 per cent in 2002, took the form of joint ventures. The services sector, in particular telecommunications and finance, accounts for the largest share of these investment flows (Chart I.3). The share of the manufacturing sector has also grown thanks to investment in industry, in particular chemicals, sugar and tobacco. The same applies to construction activities.

[8] These figures represent operational investment projects only. If all of the projects registered with the Rwanda Investment Promotion Agency (RIPA) were included, the figures would be 208.1 billion, 22.9 billion and 17.1 billion respectively. The statistics for 2001 are high because the RIPA only came into operation in 2000. These statistics are different from those contained in the balance of payments.

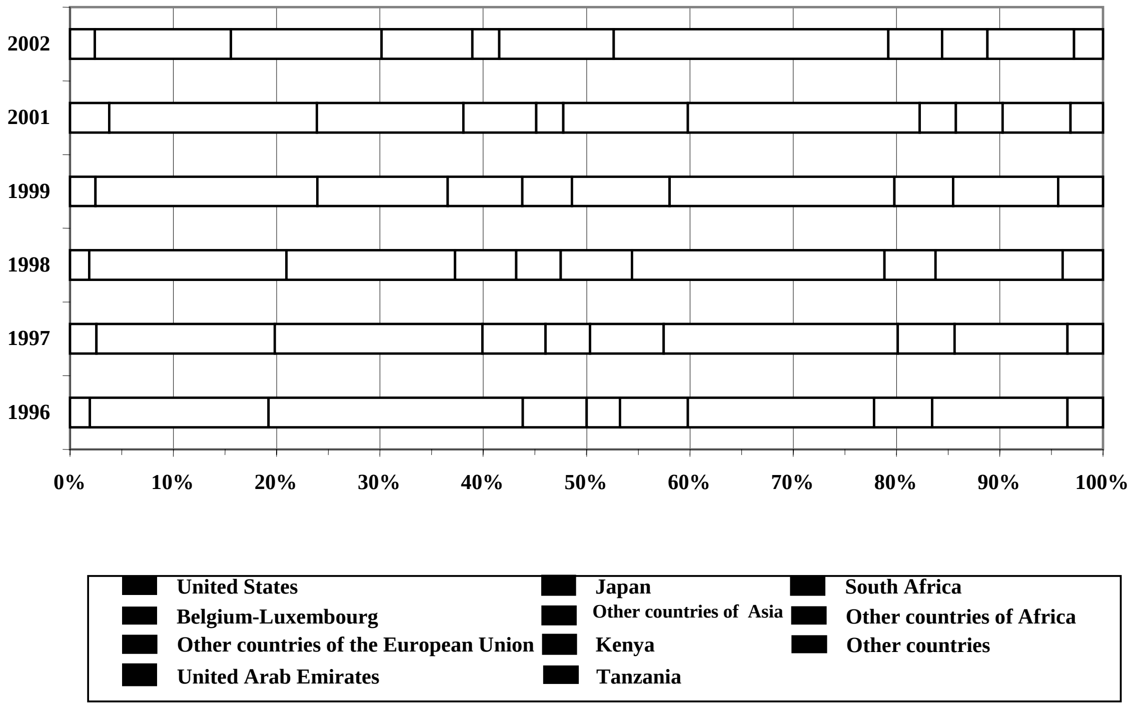
[9] UNCTAD (2002).

Chart I.2
Origin and destination of goods, 1996-2002

(a) Exports

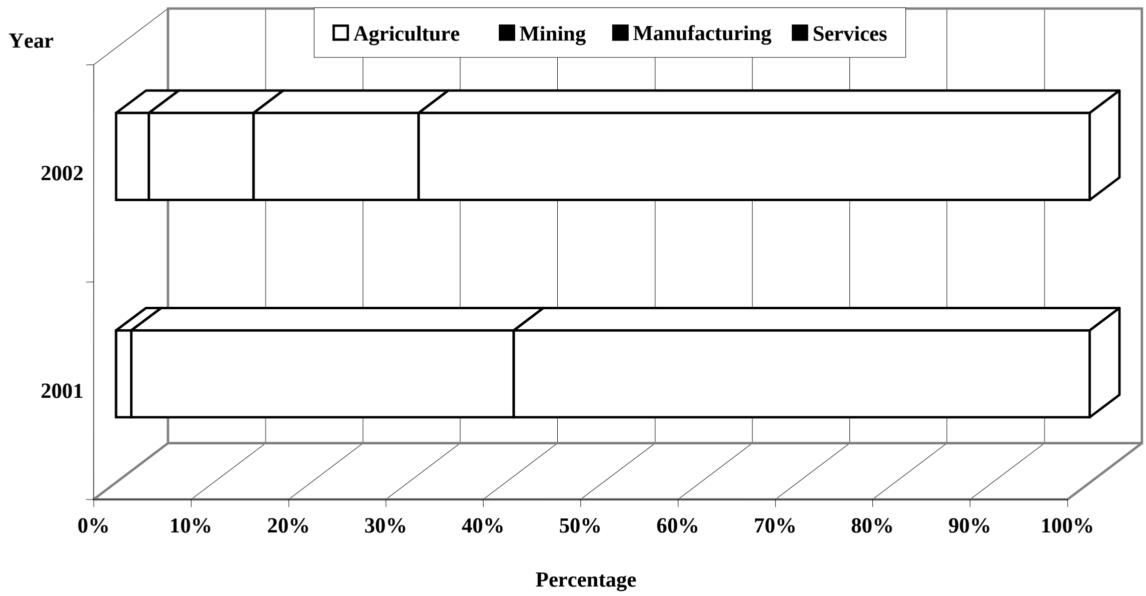


(b) Imports



Source: WTO Secretariat calculations, based on data taken from Comtrade, UNSD (SITC, Rev. 3).

Chart I.3
Sectoral distribution of foreign direct investment, 2001 and 2002



Source: WTO Secretariat, on the basis of data supplied by the Rwandan authorities.

19. Between August 2000 and December 2003, FDI reached US$49 million, with investment per project ranging from US$50,000 to US$12 million. The leading investors, in order of importance, were India, the United States, Kenya, Germany, Belgium, Canada, Great Britain, the Netherlands, Switzerland, South Africa, Lebanon and Oman.[10] These investments were directed to the manufacturing sector (16 enterprises), services, including retail trade (four enterprises), mining (two enterprises) and construction (one enterprise), and have resulted in the creation of 5,616 jobs. Among the factors which, according to the authorities, have had a positive influence on FDI are the macroeconomic and structural reforms (including the privatization programme), the introduction of the Investment Code and the setting up of a government agency (the Rwanda Investment Promotion Agency – RIPA), good governance at the State enterprise level, membership of COMESA, and the availability of cheap, semi-skilled labour. On the other hand, investment flows were considerably hampered by factors such as the high cost of energy, water and telecommunications, the lack of local raw materials and of skilled labour, and conflicts and insecurity in the Great Lakes region.

(4) OUTLOOK

20. An annual real GDP growth rate of 6 per cent is expected for the period 2004–2005, a projection which assumes the continuation of economic reforms that should limit the inflation rate to 3 per cent. A 10 per cent increase in export revenue is expected in 2004, and 7 per cent in 2005. Private investment should grow progressively to reach 18 per cent of GDP in the medium term, as against the current 12 per cent. Rwanda's debt should become sustainable (i.e. the country should

[10] In order of the number of acquisitions.

achieve a ratio of net present value of debt to exports of less than 150 per cent) as of 2008. This projection takes account of the Government's choice to finance priority expenditures relating to its poverty reduction programme through foreign loans, and assumes a sustained growth in the volume of Rwandan exports of some 11.2 per cent per year.

21. The inflationist pressures in 2003 represent a major challenge, since their frequency could discourage private investors and hence hinder growth. In order to maintain inflation at 3 per cent, measures will have to be taken to reduce the fiscal deficit. The Government plans to strengthen measures aimed at eliminating extra-budgetary expenditure and to extend the surveillance exercised by the auditor general to all ministries (on an annual basis). The withdrawal of Rwandan forces from the DRC should lead to a reduction in military expenditure. Improved tax planning on the part of the regional authorities should help to reduce their level of indebtedness and the drain on resources. "Exceptional" expenditures (linked to the consequences of the 1994 genocide) should fall to 2.2 per cent of GDP in 2004 and 1.5 per cent in 2005. Generally speaking, the planned tax measures should make it possible to reduce the deficit (excluding foreign grants) to 8.2 per cent of GDP in 2004, and 8 per cent in 2005. Not only should the strengthening of fiscal policy help to control inflation, but it should also help to contain any negative impact of tariff reforms on public revenue.

22. If the fall in export revenue were to endure, it could restrict growth and push back the date at which Rwanda's debt becomes sustainable.[11] The vulnerability of exports to external shocks and the heavy dependence of economic growth on agriculture and construction since 2001 testify to the need to diversify the structure of production and exports and to enhance the efficiency of traditional sectors. The Government intends to take steps to reduce supply-side constraints. In particular, it intends to introduce reforms (including privatization) in certain State enterprises operating in key sub-sectors such as tea and coffee, or infrastructure services (telecommunications, energy, finance); to introduce a multi-sectoral regulatory authority; to reinforce banking supervision; to establish a new legal framework for the financial sector in order to facilitate the recovery of debts; and to create commercial courts to help to enforce contracts.

[11] According to certain government estimates, the date at which the foreign debt becomes sustainable could be delayed to 2016 unless creditors take further debt relief measures.