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Senegal: Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding

December 5, 2008

The following item is a Letter of Intent of the government of Senegal, which describes the policies that Senegal intends to implement in the context of its request for a policy support instrument from the IMF. The document, which is the property of Senegal, is being made available on the IMF website by agreement with the member as a service to users of the [IMF](#) website.

LETTER OF INTENT

Dakar, Senegal
December 5, 2008

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
700 19th Street, N.W.
Washington, D.C., 20431

Dear Mr. Strauss-Kahn,

1. The attached Memorandum of Economic and Financial Policies (MEFP) reviews implementation to date of the government of Senegal's macroeconomic and structural program under the country's three-year Policy Support Instrument (PSI), approved by the IMF Executive Board on November 2, 2007. Details of this program were set out in the initial MEFP of October 3, 2007 and in the MEFP of May 30, 2008. The attached MEFP builds on the two previous Memoranda, with particular emphasis on measures and objectives for the remainder of 2008 and the first half of 2009.
2. The government requests access to the Exogenous Shock Facility (ESF) for 30 percent of quota, the equivalent of SDR 48.54 million, in two tranches. The MEFP outlines the government's policies to respond, in a sustainable manner, to the oil and food price shock that has severely affected Senegal. In particular, the government aims to strengthen agricultural production and implement energy sector reform. It has also eliminated virtually all subsidies and tax suspensions that had been introduced on a temporary basis in the immediate wake of the price shock, and will remove the remaining subsidy on butane gas by mid-2009.
3. Three quantitative assessment criteria for the second review under the PSI were not met, namely those on domestic arrears, budgetary float, and nonconcessional external borrowing. As described in the attached MEFP, the government is taking strong corrective measures to address the underlying weaknesses. In light of these actions and the observance of the other quantitative criteria and structural conditionality under the program, the government requests waivers of the missed criteria.
4. The government believes that the policies and measures set forth in the attached MEFP are sufficiently strong to achieve the objectives of the PSI program and ESF arrangement. In the government's view, the PSI remains the appropriate vehicle to maintain a close policy dialogue with the IMF, signal commitment to sound policies to the international community, and move the structural reform agenda forward. It will promptly take any additional measures necessary for the achievement of the objectives of the program. The

government will consult with the IMF—at its own initiative or whenever the Managing Director of the IMF requests such a consultation—before the adoption of any such measures or changes to the policies described in the attached Memorandum.

5. The government will provide the Fund with such information as the Fund may request in connection with the progress made in implementing the economic and financial policies and achieving the objectives of the program.

6. The government authorizes the IMF to publish this letter, the attached Memorandum, and the related Staff Report.

Sincerely yours,

/s/

Mamadou Abdoulaye Sow
Minister of Budget

Attachment: Memorandum of Economic and Financial Policies

ATTACHMENT I

MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

Dakar, December 5, 2008

I. INTRODUCTION

1. **The government remains determined to preserve macroeconomic stability, strengthen private sector-driven growth in a sustainable way, and make quick progress toward achieving the Millennium Development Goals.** To meet these objectives, the government will implement its economic and financial program, which is based on prudent macroeconomic policies and an acceleration of structural reforms. The commitments made by the government in the Memorandum of Economic and Financial Policies (MEFP) of October 3, 2007, and the MEFP of May 30, 2008, continue to anchor the policies and reforms being pursued. However, these commitments are strengthened in this MEFP, given the observed budgetary weaknesses, so as to prevent such weaknesses in the future and normalize the government's financial relations with the private sector. This MEFP describes recent economic developments, program performance, and the specific measures and objectives envisaged for the remainder of 2008 and the first half of 2009.

II. RECENT ECONOMIC DEVELOPMENTS AND PROGRAM PERFORMANCE

2. **Macroeconomic developments in 2008 were less positive than expected.** Despite a sound performance of the agricultural sector, the most recent estimates put GDP growth in 2008 at about 3.9 percent as a result of several factors: (i) the impact of the rise in food and energy prices on real domestic consumption; (ii) the delayed resumption of the operations of Industries Chimiques du Sénégal (ICS); and (iii) a slowdown in private sector activity, especially in the construction sector, related to government payment delays. Inflation is expected to be 6 percent and the current account deficit about 12¼ percent of GDP in 2008, mainly because of the large increases in international food prices and, to a lesser extent, energy prices. It is also anticipated that foreign direct investment (FDI) and aid will be adequate to finance a large portion of the balance of payments and maintain a level of reserves to cover around 3½ months of imports.

3. **Budget execution has run into major problems.** The difficulties became apparent as a result of Policy Support Instrument (PSI) program measures, in particular: (i) the structural assessment criterion on extending the coverage of the integrated expenditure tracking system (SIGFIP) to the payment phase, (ii) the structural benchmark concerning the audit of payment delays by the financial audit inspectorate (IGF) of the Ministry of Finance, and (iii) the broadening of the definition of the quantitative assessment criterion on the budgetary float. Follow-up work by Ministry of Finance staff has allowed the authorities to

estimate that the stock of payment delays at end-October 2008 amounted to CFAF 174.9 billion (3 percent of GDP) for the regular budget, CFAF 50 billion (3/4 percent of GDP) in Treasury corresponding accounts (*comptes de correspondants du Trésor*), and CFAF 74 billion (1¼ percent of GDP) of extrabudgetary expenditures, of which by the line ministries CFAF 11 billion, agencies CFAF 31.3 billion, public health institutions CFAF 12.1 billion, and universities CFAF 19.1 billion.

4. **The government acknowledges that these amounts result from expenditures that were too high considering the availability of financing and the macroeconomic circumstances prevailing in the country during 2006–08.** Three factors explain the problems:

- First, after the surge in oil and food prices the government decided to maintain high energy subsidies (for electricity and butane gas) to protect household purchasing power and, in July 2007, to suspend duties and taxes on some basic staples. This sharply reduced the budgetary room for maneuver. In March 2008, direct subsidies were introduced on rice and cooking oil. All in all, the subsidies on oil and food products represented 7 percent of GDP for the years 2006 to 2008 combined.
- Second, despite the crowding-out pressures from the financial support for oil and food products, the government maintained the implementation speed of its wide-ranging public investment program during the period. This program centers on infrastructure development as an essential pillar for the promotion of growth and success of the poverty reduction strategy (PRSP); it helped sustain economic activity and employment.
- Finally, the frequent use of Treasury advances to undertake spending that not been initially budgeted helped exacerbate cash flow pressures during the budget year. All in all, public expenditure representing 5½ percent of GDP was executed through Treasury advances in 2006–08, thus reducing available resources for other expenditure.

5. **Because of these problems, the government was unable to observe three quantitative assessment criteria: on domestic arrears, the budgetary float, and nonconcessional external borrowing.** The nonobservance of the first two criteria resulted directly from the budgetary slippages, while the criterion on nonconcessional external borrowing was intentionally breached to implement the action plan (see paragraph 14) and correct the budgetary slippages. Given the low liquidity in the regional financial market, the government had to resort to nonconcessional external financing to repay the private sector quickly and, thereby, boost economic activity. The government had to do this as the alternative of maintaining a large stock of payment delays would have been harmful to the economy in an already difficult period and would, at any rate, have led to the nonobservance

of another assessment criterion, on the budgetary float at end-December 2008. The government is seeking waivers from the IMF Executive Board for the noncompliance with these three assessment criteria in view of the strong corrective measures proposed below.

6. **The government confirms, however, that it has observed the other quantitative criteria of the program.** It has not accumulated external arrears throughout the program period. The basic fiscal balance was observed at end-September 2008, as was the indicative ceiling on the share of public sector contracts awarded by single tender, which was contained at 17 percent by end-June and 19 percent by end-September.

7. **In 2008, the government continued its efforts to safeguard social sector spending.**¹ The fiscal adjustment measures that reduced expenditure by CFAF 191 billion relative to the appropriations approved by the National Assembly in the context of the initial 2008 Budget Law did not affect social sectors. The government plans to increase the total social sector share of the national budget from 32.6 percent in 2007 to 35.9 percent in 2008. It also intends to request technical expertise from the World Bank and other development partners with sectoral expertise to help improve its analysis of the efficiency of social sector spending.

8. **The government has made significant progress in implementing its structural reform program.** All structural assessment criteria and benchmarks had been observed by end-October 2008:

- A plan for issuing treasury bills and government securities was finalized in mid-August, six weeks later than scheduled. The plan is expected to help the Ministry of Finance improve its forecasting of cash flow needs and accustom the market to regular issuances;
- A new electricity tariff structure was adopted at the beginning of August. This is expected to help the national electricity company, SENELEC, restore its financial equilibrium and encourage consumers to save electrical power. The rate increases, which averaged 17 percent, were asymmetrical and relatively small for low-income consumers;
- An audit of domestic payment delays was completed by IGF on September 30, as planned;

¹ Social sector spending, as defined in the program, is PRSP expenditure. It includes expenditure on health, education, justice, social development, environmental affairs, rural water works, and sanitation.

- The Council of Ministers adopted, by end-October, all laws and regulations to ensure the effective transfer of direct tax collection responsibilities from the Treasury to the Revenue Authority (DGID);
- In addition, a Prime Minister's circular aimed at improving the system for planning, monitoring, and evaluating public investment was sent to all sectoral ministries and independent executing agencies on November 13, 2008. The circular sets out procedural and institutional rules to ensure: (i) consistency among the various investment projects and between them and strategic objectives; (ii) compatibility between the investment programs and the medium-term macroeconomic framework; and (iii) the establishment and observance of project analysis rules that vary depending on the size of the project, with the aim of selecting the best among them.

III. MACROECONOMIC POLICIES FOR 2009–10

9. **The 2009–10 macroeconomic outlook is framed by a relatively unfavorable international environment.** This includes a slowdown in global growth, problems on the financial markets, and the continued rise in food prices. Nevertheless, the government anticipates that the specific structure of the Senegalese economy, combined with the economic policy intentions described below, as well as the elimination of payment delays, will offset the effects of the negative international environment.

- *Real GDP growth is projected to average about 5½ percent over the next two years.* This projection is based on the gradual resumption of ICS's production, recovery in private sector activity linked to the elimination of payment arrears, and FDI-related economic growth.
- *Inflation is expected to return to its historical level of 2 percent over the medium term.* Given the pressures, albeit abating, on food prices over the short term, the government forecasts an inflation rate of 3¼ percent in 2009. The subregional framework governing monetary and foreign exchange policies will continue to help keep inflation low, based on the peg to the euro. Although the sound performance of the agricultural sector is expected to help reduce inflationary pressures, a prudent fiscal policy will remain the key instrument for achieving macroeconomic stability in Senegal and contributing to the WAEMU's external stability.
- *The external current account deficit is projected to fluctuate between 11 percent and 12 percent of GDP and be increasingly financed by FDI flows.* External and domestic public debt would increase slightly to about 23 percent and 7 percent of GDP, respectively, by 2010.

A. Fiscal Policy

Fiscal stance

10. **The government reiterates its commitment to limiting the overall fiscal deficit to 4 percent of GDP over the medium term.** A deficit of this size will help ensure continued debt sustainability. This will be key for supporting investment and growth, as well as for helping to maintain domestic stability while containing demand pressures and preventing crowding out of the private sector.

11. **The deficit will be temporarily lowered to 3.3 percent of GDP in 2008 because of the need to settle payment delays related to 2007 expenditure.** The deficit target will be consistent with a basic fiscal deficit of CFAF 21 billion in 2008 (revised quantitative assessment criterion).

12. **The government will keep the 2009 fiscal deficit to less than 3 percent of GDP.** Parliament will pass a 2009 Budget Law that is consistent with the budgetary projections of the macroeconomic framework agreed with the IMF under the PSI (prior action). This will help ensure that appropriations for each ministry (or any other spending body) are consistent with available resources and other macroeconomic objectives of the program. In line with the overall deficit target for 2009, the basic fiscal surplus is expected to exceed CFAF 5 billion at end-June 2009 (quantitative assessment criterion). This surplus is necessary to complete the settlement of all past payment delays.

13. **Despite the envisaged fiscal adjustment, expenditure in priority sectors will continue to grow.** This should enable the government to increase social spending to 39.2 percent of total expenditure, or 10.5 percent of GDP, by 2010. Social sector spending will reach 9.2 percent of GDP in 2008 and 9.9 percent of GDP in 2009. Expenditure for rural parts of the country and on infrastructure will also be increased. Finally, to facilitate the monitoring of HIPC and MDRI expenditure, the government has expanded the mechanism for identifying such expenditure, which should allow better monitoring in 2009.

Elimination of payment delays

14. **Given the negative impact on private sector activity of the payment delays, in August 2008 the government adopted an action plan aimed at rapidly turning the situation around.** The action plan has since been strengthened and now covers several key aspects:

a. The 2008 supplementary budget law passed on November 27, 2008, (i) regularized Treasury advances executed during the year and transfers of appropriations that exceeded the 10 percent threshold authorized by the Organic Budget Law; and (ii) reduced by CFAF 191 billion the appropriations initially approved by parliament to take account of

revenue shortfalls and incorporate the effect of the expenditure reductions announced by the Prime Minister's circular of May 2008 and the additional reductions of CFAF 100 billion described in the action plan.

- b. The government is currently formulating financing options to reduce the budgetary float.
- c. To create budgetary room, the government has eliminated all budgetary subsidies on food products. This includes elimination of the subsidy on rice as of October 29, 2008; reinstatement of the previously suspended duties and taxes on other food products as of September 15, 2008; and removal of the specific tax on vegetable oils as of September 15, 2008.
- d. The government has undertaken to curtail and then completely eliminate the subsidy on butane gas by end-June 2009, as well as to revise the electricity pricing method (see paragraph 33a).
- e. The increase in the levy on alcohol and cigarettes is expected to take effect by end-December 2008.
- f. The government will launch tenders for the privatization of Hotel Méridien Président in the first quarter of 2009 and expects to finalize renegotiation of the second mobile telephone license in 2009.
- g. The government will launch technical audits of all extrabudgetary expenditure by end-December 2008, as described in paragraph 26 below.
- h. A major exercise of data reconciliation and verification has been completed by the Treasury, as described in paragraph 24. It will enable the Ministry of Finance to reconcile its data with those of the private sector.
- i. As stated below, the government has also committed to taking strong corrective measures to restore the quality and transparency of the budgetary system, prevent new budgetary slippages and, more generally, make public financial management systems compliant with best international practices over the medium term.

15. With a view to quickly regularizing its financial relations with the private sector and preventing the recurrence of budgetary slippages, the government undertakes to:

- a. Eliminate domestic payment arrears, as defined by the WAEMU, by end-December 2008 and continuously maintain a zero balance thereafter;

- b. Limit the stock of the budgetary float, defined as expenditure for which bills have been received and validated but not yet paid by the Treasury, to a ceiling of CFAF 92 billion at end-2008 (quantitative assessment criterion);
- c. Limit the stock of committed expenditure for which bills have not yet been validated, and strengthen the link between monthly commitments at the level of the sectoral ministries and the availability of cash; and
- d. Meet the new quantitative assessment criterion under the program envisaging a zero limit on Treasury advances (to be observed continuously). Expenditures that are not subject to regular budget execution procedures, but are authorized by Advance Decree in line with paragraph 11 of the TMU, are not considered Treasury Advances

Debt management

16. **To ensure debt sustainability, the government will continue to adhere to the general principle of not contracting or guaranteeing external loans on nonconcessional terms.** However, as the government has not yet managed to raise funds totaling about CFAF 80 billion for the Dakar-Diamniadio toll highway because of the difficult situation on international markets, this amount will be raised in the first half of 2009 so that donor resources can be quickly supplemented with the government's financial contribution under the public-private partnership (quantitative assessment criterion). Several feasibility studies, in particular by the World Bank and the French development agency, have shown that the yield of this project is higher than the cost of the government's nonconcessional borrowing. The government will consult with IMF staff well in advance for any further exceptions to this quantitative assessment criterion. Any proceeds from asset sales will in the first place be used to accelerate the settlement of payment delays, extrabudgetary spending accepted by the Ministry of Finance on the basis of technical audits, and repayment of nonconcessional external loans contracted in 2008-09.

17. **In accordance with earlier commitments, other aspects of debt management will also be strengthened.** First, every quarter or after each issuance, the government will, in consultation with the BCEAO, update the rolling two-year government securities issuance program. Based on the macroeconomic framework of the PSI, the government plans to issue CFAF 30 billion in securities in December 2008 and in each quarter of 2009; it will also update its rolling two-year plan after each issuance. Second, as of December 2008, the half-yearly public debt sustainability analysis will include a study of the risks from contingent liabilities—related to guarantees issued by the government, to PPPs, and to the operations of public enterprises. Finally, the government has requested assistance from the U.S. Treasury to strengthen its debt management capacity. It has also asked the major rating agencies (Standard and Poor's, Fitch, and Moody's) to rate Senegal's country risk so that it can identify the principal sources of weakness and take appropriate remedial measures.

IV. STRUCTURAL REFORMS

A. Fiscal Reforms

18. **The government recognizes that the shortcomings in budget planning, execution, and monitoring, as revealed by recent budgetary slippages, must be urgently corrected.** This is key to preserving macroeconomic stability, enhancing the efficiency of public spending, ensuring the integrity of the budgetary and accounting systems, and increasing fiscal transparency. The measures described below, based on an IMF technical assistance mission, aim at meeting those objectives and are expected to help prevent the reappearance of past problems. The government will make every effort to implement the recommendations of the technical assistance report, which will be integrated in its public finance reform framework.

Budget planning

19. **Before January 31, 2009, the government will establish by decree the timetable and the main methods for budget formulation, which will be used for the first time for the preparation of the 2010 budget (structural assessment criterion).** This will involve, in particular: (i) the preparation of an initial macroeconomic framework by end-March; (ii) the formulation of the government's major economic and fiscal priorities (previous year's budget execution figures, growth forecasts, government revenue and expenditure projections, estimated civil service staffing developments, and other relevant budgetary and financial aggregates) for the fiscal policy debate in parliament, which is to take place by June at the latest; (iii) the establishment of medium-term sectoral expenditure frameworks with a top-down constraint (i.e., expenditure ceilings by ministry and any other administrative unit receiving budgetary appropriations); and (iv) the preparation of a second (updated) macroeconomic framework by end-August for the formulation of the draft budget law.

20. **In 2009 the government will introduce two supplementary budgets, one in the middle of the year and one towards the end, or at least one supplementary budget at mid-year.** This will make it possible to regularize transfers of appropriations (see paragraph 22) and any extrabudgetary expenditures that the government decides to recognize on the basis of technical audits (see paragraph 26). These supplementary budgets will also regularize all decrees issued for implementation of articles 12, 15, and 18 of the 2001 Organic Budget Law, and revise the estimated use of appropriations (*crédits évaluatifs*) based on the latest available information. The extent of regularization of extrabudgetary spending accepted by the government based on technical audits will also take into account the availability of resources in 2009; in any case, any remaining regularizations will be undertaken in 2010. The government plans to implement the procedure of two supplementary budgets every year.

Budget execution

21. **As stated earlier, Treasury advances, which have no legal basis and were one of the reasons for the recent budgetary problems, will be eliminated.** The government issued a decree to supplement the general regulation on public accounting (RGCP). The decree limits expenditure execution to the normal and simplified procedures only and prohibits the use of any other type, in particular Treasury advances (completed prior action).

22. **The government will simplify the system for reopening and carrying over budgetary appropriations and commitments by issuing an implementation decree for articles 17 and 18 of the organic budget law before the end of the complementary period on February 28, 2009 (structural assessment criterion).** The current system is excessively complex and too widely used, to the detriment of the principle of annual budgeting and the preservation of macroeconomic stability. The decree will abolish the possibility to reopen appropriations and will set out the system for carrying them over as follows: (i) any capital budget appropriations for which a payment order has not been issued at the end of the complementary period may be carried forward to the subsequent budget year, by order issued no later than 30 days after the end of the complementary period, within an overall ceiling of 5 percent of the total capital budget for the current year (leaving open the choice between carrying out investment planned for the previous year and the current year); (ii) appropriations (*crédits de paiement*) that are carried over are canceled in the initial budget year and added to the appropriations for the subsequent budget year; (iii) appropriations related to expenditure for which bills have already been received and validated (*dépenses liquidées*) are automatically carried forward, within the above-mentioned ceiling; and (iv) appropriations not carried forward become unusable. The mid-year supplementary budget law will ensure conformity with the macroeconomic framework agreed with the IMF. In addition, within this new framework, the government will issue an administrative order by March 31, 2009, to definitively settle the reopened and carried-over amounts of appropriations from all budget years prior to 2008, to be borne in the 2009 budget year.

23. **To more systematically implement closure provisions for budget execution and accounting, the government issued a circular recalling the deadlines.** A failure to effectively and expeditiously stop budgetary operations for a given year complicates management of the government's financial position. It also delays compilation of account statements, prevents the accurate assessment of amounts carried forward from one year to the next, undermines the budgeting for subsequent years, and complicates the government's cash flow management. To be able to comply with the required deadlines for the production of documents monitoring the implementation of fiscal policy, the government undertakes to reduce the time allowed for commitments (*engagements*) by setting the cutoff date at November 30. The complementary period stipulated in the laws, which halts the administrative phase of budget execution (issuance of payment orders) on December 31, and the accounting phase at end-February of the subsequent year, will be applied. Beyond

February 28, any operation from the previous budget year with an impact on government cash flow must be imputed to the accounts for the current year. A reminder of these measures was issued in a Ministry of Finance circular. The SIGFIP data will be frozen and published in detail on the Ministry of Finance website by April 30 (structural assessment criterion). Any accounting adjustments made after April 30 must be recorded in the following budget year.

Accounting system and budgetary monitoring

24. **The government, in consultation with the IMF, established a detailed procedures manual for reconciling data between the fiscal reporting table (TOFE), the Treasury accounts, the net government position (NGP), and SIGFIP, and between the Treasury accounts and SIGFIP, and published the reconciliation tables for December 2007 and March, May, June, July, August, and September 2008 (completed prior action).** This reconciliation will facilitate the rapid detection of budget management problems and increase the accuracy and reliability of the entire budget execution monitoring system. The reconciliation tables were shared with IMF staff and published on the Ministry of Finance website as soon as they were completed. This exercise of reconciliation and publication will subsequently be carried out on a quarterly basis.

25. **The government will make every effort to improve SIGFIP as a key budget monitoring system.** To that end, the government will undertake an audit of SIGFIP during the first half of 2009 to ensure that each type of expenditure is thoroughly tracked in the system and with the aim of establishing genuine administrative accounting (*comptabilité administrative*), based on SIGFIP. The government may request technical assistance from the IMF for this audit.

Extrabudgetary expenditure

26. **The IGF audit that led to the identification of CFAF 74 billion in extrabudgetary expenditure will be followed up.** An independent external audit will analyze the circumstances under which these commitments were generated. The audit will also analyze the possible existence of additional spending without budgetary lines in addition to the amounts identified by the IGF audit. The terms of reference of this audit will be drawn up in consultation with IMF staff. The audit report will be submitted to IMF staff by end-March 2009 (structural benchmark). No payments will be made to the private sector for any extrabudgetary expenditure before the audit has established the nature of claims and specified the goods and services that were provided and their unit cost. To prevent a recurrence of such spending, the government will impose sanctions on employees found to be at fault and apply a discount factor to the claims of private firms that agreed to provide goods or services on unlawful terms. The government will pay claims recognized on the basis of the audit only after authorization by a budget law providing for simultaneous reductions of appropriations for other expenditure items.

27. **The compilation of the government's Treasury accounts and budget review laws will be accelerated.** For this purpose:

- The Treasury accounts for FY 2006 will be forwarded to the Audit Court by end-January 2009, those for FY 2007 by end-March 2009, and those for FY 2008 by end-July 2009, as legally stipulated; and
- The draft budget review laws for FY 2004, FY 2005, FY 2006, and FY 2007 will be sent to the Audit Court by, respectively, end-December 2008, end-February 2009, end-May 2009, and end-June 2009.

Government procurement

28. **A new government procurement framework has been in place since January 1, 2008. The government is determined to apply it rigorously.** The principles described in the previous Memorandum remain valid. In particular:

- a. The government will meet the quarterly indicative target on the share of government contracts awarded by single tender, set at 20 percent of all contracts, including those entered into by agencies and other government bodies;
- b. The government will continue to publish the list of contracts awarded each quarter on the website of the central directorate for public procurement (DCMP);
- c. No public procurement will be allowed unless it has been included in the procurement plans submitted to the DCMP; and
- d. The procurement regulatory agency (ARMP) will conduct audits and surveys of government contracts, as stated in the previous MEFP. The first audit report for 2008 will be published by May 31, 2009 (structural benchmark).

Large investment projects

29. **The government intends to continue to ensure transparency and efficiency in the implementation of large public investment projects.** It deems them essential for increasing the growth potential of the Senegalese economy.

30. **Earlier commitments regarding the airport project and the Dakar integrated special economic zone (DISEZ) will be met.** In particular, the government will prepare memoranda of understanding spelling out the respective rights and duties of APIX, DGID, and DGD with respect to the management of DISEZ, including conflict resolution rules. They will also describe, among other things, specific measures for combating fraud and tax evasion (structural benchmark for end-March 2009).

Social safety net for the rise in prices

31. **Helping the population deal with the rise in food and energy prices is a national priority.** The government is therefore adopting a balanced approach between the preservation of macroeconomic stability and emergency measures for the needy. This follows the government's decision to eliminate the subsidies and reverse the suspension of customs duties and taxes on certain staples, and to remove the special tax on vegetable oils. More specifically, the government will help the most underprivileged segments of the population through the following measures:

- Expansion of the school meals program. This measure will have a positive impact on the purchasing power of households as well as on enrollment rates and the performance of children in school;
- Feasibility study regarding the introduction of a subsidy on public transportation; and
- Request for technical expertise from the World Bank to analyze the operational feasibility of introducing a targeted program of cash transfers to the poorest households, as recommended by the IMF's Poverty and Social Impact Analysis (PSIA) mission.

32. **In the long run, the government will focus on improving the supply and reducing the costs of energy and food products.** The agricultural sector is also important for poverty reduction. The government deems it important to increase domestic agricultural production, in particular of high-yield products such as rice. It will therefore work with farmers to improve infrastructure, especially irrigation and storage systems; increase competition; and restructure subsidies with a view to enhancing agricultural productivity. Similarly, energy sector reform aims at boosting production and generating cost reductions that the government plans to gradually pass on to consumers.

Energy sector reform

33. **Energy sector reform is crucial for improving the supply of energy to the economy and containing fiscal risks.** The government has started implementing its program of reforms, supported by the World Bank and other donors, as stated in the sectoral policy letter. The government will apply the principle of market-based pricing and of implementing energy saving and efficiency measures. In support of this program, the government will:

- a. Modify the structure of electricity tariffs every three months and adjust the institutional price setting process;
- b. Complete the recapitalization of SENELEC by mid-2009; CFAF 9 billion will be appropriated in 2009 for this purpose; and

c. Eliminate the subsidy on butane gas by end-June 2009. To this end, butane gas prices will be adjusted, so that the annual subsidy can be limited to CFAF 32 billion in 2008 and CFAF 8 billion in 2009.

B. Accelerated Growth Strategy and Development of the Private Sector

34. **The Accelerated Growth Strategy (AGS) will remain the anchor for the agenda of reforms and priority actions to enhance the growth potential of the Senegalese economy.** The government will continue to adopt a participative approach in the implementation of this strategy, especially with respect to the five cluster sectors. To this end, as stated in the implementation decree of the AGS law, the monitoring committee chaired by the Prime Minister will meet every six months, and the technical committee chaired by the Minister of Finance will meet every three months.

35. **Since the seventh meeting of the Presidential Investment Council (CPI) in November 2007, Senegal has carried out significant reforms to improve the business climate.** The most salient of these have been: (i) simplifying import and export procedures, simplifying customs clearance procedures, and reducing the time and costs for formalities; (ii) simplifying property transfer procedures, with wait times reduced from 114 days to 18 days; (iii) simplifying the procedures for granting building permits, certificates of compliance and other requirements, with wait times reduced from 217 days to 78 days; (iv) passing the law on the promotion and development of small and medium-sized enterprises; (v) improving the legal and judicial framework, especially by increasing the number of magistrates and court clerks; (vi) improving the legal framework applicable to PPPs, for the implementation of infrastructure projects, with the amendment of the law on construction contracts, operations, and infrastructure transfers; (vii) adopting the regulations for implementation of the Labor Code; and (viii) creating new technical and vocational education centers.

36. **In the context of the November 2008 CPI, the government has committed to taking action in several key areas.** These include: (i) updating and modernizing labor legislation, (ii) strengthening vocational education, and (iii) taking stock of the tax system and incentives for the emergence of new methods of financing the private sector, such as leasing, factoring, and venture capital.

C. Financial Sector Reforms

37. **The government is determined to safeguard the soundness of the financial system and enhance its contribution to the economy.** In accordance with its previous commitments, the government therefore intends to:

- a. Implement all the decisions and recommendations of the WAEMU Banking Commission;
- b. Act in close cooperation with the BCEAO and the WAEMU Banking Commission to limit the impact of the ICS restructuring plan on the banking system and the budget;
- c. Carefully monitor all the potential effects of the global financial crisis on the soundness and liquidity of the Senegalese banking system and the regional financial markets, in close cooperation with the BCEAO, the regional Banking Commission, and the banks' home-country supervisors;
- d. Adopt, by end-January 2009, the implementation decree for the new law on microfinance institutions that became effective on September 3, 2008 (structural benchmark), and continue to strengthen the supervision unit of the Ministry of Finance;
- e. Submit to Parliament the new legislation on combating the financing of terrorism by end-December 2008; and
- f. Continue establishing a legal framework to encourage private sector access to a diversified supply of credit.

VI. PROGRAM MONITORING

38. Quantitative assessment criteria for end-December 2008 and end-June 2009 and quantitative indicative targets for end-March and end-September 2009 were set to monitor program implementation in 2008-09 (see Table 1 in the attached technical memorandum of understanding (TMU)). These program targets will also apply to the ESF. The government and IMF staff also agreed on the prior actions, structural assessment criteria, and structural benchmarks listed in Table 2 of the TMU. The third and fourth reviews under the PSI are scheduled to take place, respectively, by end-June 2009 and end-December 2009, and the first review under the ESF by end-June 2009. The government understands that completion of the third review of the program is contingent upon observance of the assessment criteria set for end-December 2008 and the structural assessment criteria for the period through April 30, 2009.

ATTACHMENT II

TECHNICAL MEMORANDUM OF UNDERSTANDING

Dakar, December 5, 2008

1. This technical memorandum of understanding (TMU) defines the quantitative and structural assessment criteria, indicative targets, and structural benchmarks on the basis of which the implementation of the Fund-supported program under the Policy Support Instrument (PSI) will be monitored in 2008 and 2009. The quantitative program targets will also serve as performance criteria under the ESF. The TMU also establishes the terms and timeframe for transmitting the data that will enable Fund staff to monitor program implementation.

I. PROGRAM CONDITIONALITY

2. The quantitative assessment criteria for December 31, 2008 and June 30, 2009 and the quantitative indicative targets for March 31, 2009, are shown in Table 1. The prior actions, structural assessment criteria, and structural benchmarks established under the program are presented in Table 2.

II. DEFINITIONS, ADJUSTERS, AND DATA REPORTING

A. The Government

3. Unless otherwise specified below, the government is defined as the central administration of the Republic of Senegal and does not include any local administration, the central bank, or any government-owned entity with a separate legal personality (e.g., public universities and hospitals).

B. Basic Fiscal Balance (Program Definition)

Definition

4. The basic fiscal balance (program definition) is the difference between the government's budgetary revenue and total expenditure and net lending, excluding externally-financed capital expenditure (financed by donors), drawings on on-lent loans (except on-lent loans to the energy sector financed through donor budget support), and expenditure funded with HIPC- and MDRI-related resources. Budgetary revenue excludes privatization receipts and sales of mobile telephone licenses or other government assets. Government expenditure is defined on the basis of payment orders accepted by the Treasury (*dépenses prises en charge par le Trésor*). The assessment criterion is set as a floor on the cumulative basic fiscal balance since the beginning of the year.

Example

5. The floor for the basic balance (program definition) as at December 31, 2008 is minus CFAF 21 billion. It is calculated as the difference between budgetary revenue (CFAF 1209 billion) and total expenditure and net lending (CFAF 1541 billion), excluding externally financed capital expenditure (CFAF 226 billion), drawings on on-lent loans (CFAF 5 billion), and expenditure funded with HIPC- and MDRI-related resources (CFAF 79 billion).

Reporting requirements

6. During the program period, the authorities will report monthly to Fund staff provisional data on the basic fiscal balance (program definition) and its components with a lag of no more than 30 days. Data on revenues and expenditure that are included in the calculation of the basic fiscal balance, and on expenditure financed with HIPC- and MDRI-related resources, will be drawn from preliminary treasury account balances. Final data will be provided as soon as the final balances of the treasury accounts are available, but not later than two months after the reporting of the provisional data.

C. Government Domestic Payment Arrears**Definition**

7. In line with the WAEMU definition, domestic payment arrears are government expenditures cleared for payment (*dépenses ordonnancées*) but not paid during a period of 90 days after the date the payment order (*ordonnancement*) was cleared. The assessment criterion on domestic payment arrears will be monitored until the time of the second PSI review on a continuous basis and discontinued thereafter.

Reporting requirements

8. The authorities will report to Fund staff any accumulation of domestic payment arrears, as defined above, as soon as incurred.

D. Budgetary Float**Definition**

9. The budgetary float (*instances de paiement*) is defined as the outstanding stock of government expenditure for which bills have been received and validated but not yet paid by the Treasury (the difference between *dépenses liquidées non encore ordonnancées* and *dépenses payées*). The assessment criterion is set as a ceiling on the budgetary float, monitored at the end of the quarter.

Reporting requirements

10. The authorities will report to Fund staff on a weekly basis (i.e., at the end of each week), and at the end of each month, a table from the expenditure tracking system (SIGFIP) showing all committed expenditures (*dépenses engagées*), all certified expenditures that have not yet been cleared for payment (*dépenses liquidées non encore ordonnancées*), all payment orders (*dépenses ordonnancées*), all payment orders accepted by the Treasury (*dépenses prises en charge par le Trésor*), and all payments made by the Treasury (*dépenses payées*). The SIGFIP table will exclude delegations for regions and embassies and treasury advances (separating regularized and nonregularized), which will be provided in a separate table. The SIGFIP table will also list any payments that do not have a cash impact on the Treasury accounts.

E. Spending Undertaken Outside of Simplified and Normal Procedures

11. This criterion is applied on a continuous basis to any procedure other than simplified and normal procedures to execute spending, including in particular Treasury advances. It only excludes spending undertaken on the basis of an advance decree for absolute urgency and need in the national interest, based on Article 12 of the Organic Budget Law. Such spending requires signatures by the President and Prime Minister. The criterion is monitored effective the time of the second PSI review.

12. The authorities will report to Fund staff on a monthly basis and with a maximum delay of 30 days any such procedure, together with the SIGFIP table defined in paragraph 10.

F. Government External Payment Arrears

Definition

13. External payment arrears are defined as the sum of payments owed and not paid on the external debt contracted or guaranteed by the government. The definition of external debt given in paragraph 15 is applicable here. The assessment criterion on external payment arrears will be monitored on a continuous basis.

Reporting requirements

14. The authorities will report to Fund staff any accumulation in external payment arrears as soon as the due date is passed.

G. Contracting or Guaranteeing of New Nonconcessional External Debt by the Government

Definition

15. This assessment criterion applies not only to debt as defined in Point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Executive Board Decision No. 6230-(79/140), last amended by Executive Board Decision No. 12274-(00/85), adopted August 24, 2000, but also to commitments contracted or guaranteed by the government for which funds have not been received. The criterion does not apply to:

- (i) CFAF debt contracted or guaranteed by the government with WAEMU residents;
- (ii) CFAF debt initially contracted or guaranteed by the government with WAEMU residents subsequently acquired by nonresidents;
- (iii) CFAF government or government-guaranteed debt where the agreement is between the government and a resident WAEMU entity and there is no ensuing contractual obligation between the government and a nonresident entity, regardless of whether the resident WAEMU entity resells the debt to a non-resident;
- (iv) debt rescheduling transactions of debt existing at the time of the approval of the PSI; and
- (v) external debt contracted by the airport project company (AIDB) to finance construction of the new Dakar Airport.

16. This criterion is measured on a cumulative basis since the approval of the second program review and applies continuously. The ceiling is raised to accommodate CFAF 80 billion to finance exclusively the Dakar-Diamniadio toll highway project. No adjuster will apply to this criterion.

17. For purposes of this assessment criterion, government is understood to include the government as defined in paragraph 3 above, as well as public institutions of an industrial and commercial nature (EPIC), public administrative institutions (EPA), public institutions of a scientific and technical nature, public institutions of a professional nature, public health institutions, local administrations, public enterprises, and government-owned or controlled independent companies (*sociétés nationales*) (i.e., public enterprises with financial autonomy where the government holds at least 50 percent of the capital), and government agencies.

18. Any external debt of which the present value, calculated with the reference interest rates mentioned hereafter, is greater than 65 percent of the nominal value (grant element of less than 35 percent) is considered nonconcessional, with the exception of IMF lending under the Poverty Reduction and Growth Facility, which is considered concessional even if it does not meet the 35 percent grant element threshold. For debt with a maturity of more than

15 years, the ten-year reference market interest rate, published by the OECD, is used to calculate the grant element. The six-month reference market rate is used for debt with shorter maturities.

Reporting requirements

19. The government will report any new external borrowing and its terms to Fund staff as soon as external debt is contracted or guaranteed by the government.

H. Public Sector Contracts Signed by Single Tender

Definition

20. Public sector contracts are administrative contracts, drawn up and entered into by government entities subject to the procurement code, for the procurement of supplies, delivery of services, or execution of work. Public sector contracts are considered single-tender contracts when the contracting agent signs the contract with the chosen contractor without competitive tender or award. The quarterly indicative target will apply to public sector contracts examined by the *Commission Nationale des Contrats de l'Administration* (CNCA) until December 31, 2007, and to those examined by the *Direction Centrale des Marchés* (DCM) thereafter.

Reporting requirements

21. The government will report quarterly to Fund staff, with a lag of no more than one month from the end of the observation period, the total value of contracts signed by all ministries and agencies and the total value of all single-tender contracts signed by these ministries and agencies.

III. ADDITIONAL INFORMATION FOR PROGRAM MONITORING

22. The authorities will report to Fund staff the following, with the maximum time lags indicated:

- (a) Effective immediately: any decision, circular, edict, decree, ordinance, or law having economic or financial implications for the current program;
- (b) With a maximum lag of 30 days, preliminary data on:
 - Tax receipts and tax and customs assessments by categories, accompanied by the corresponding revenue collected by the Treasury on a monthly basis;
 - The monthly amount of expenditures committed, certified, and for which payment orders have been issued;

- The quarterly report of the Debt and Investment Directorate (DDI) on execution of investment programs;
- The monthly preliminary government financial operations table (TOFE), based on the Treasury accounts (*balances de compte*);
- The provisional balance of the Treasury accounts; and
- A reconciliation table between the fiscal reporting table (TOFE), the Treasury accounts (identifying the relevant accounts and amounts), the net government position (NGP), and the SIGFIP on a quarterly basis.

(c) Final data will be provided as soon as the final balances of the treasury accounts are available, but not later than one month after the reporting of provisional data.

23. During the program period, the authorities will report to Fund staff provisional data on a monthly basis on current nonwage non-interest expenditures and domestically financed capital expenditures executed through advance payments and treasury advances, with a lag of no more than 30 days. The data will be drawn from preliminary consolidated treasury account balances. Final data will be provided as soon as the final balances of the treasury accounts are available, but no more than one month after the reporting of provisional data.

24. The government will report to Fund staff:

- The monthly balance sheet of the Central Bank, with a maximum lag of one month;
- The consolidated balance sheet of banks with a maximum lag of two months;
- The monetary survey, on a quarterly basis, with a maximum lag of two months;
- The lending and deposit interest rates of commercial banks, on a monthly basis; and
- Prudential supervision and financial soundness indicators for bank and nonbank financial institutions, as reported in the Table entitled *Situation des Etablissements de Crédit vis-à-vis du Dispositif Prudentiel* [*Survey of Credit Institutions in Relation to the Prudential Framework*], on a quarterly basis.

The government will update monthly on the website used for this purpose the amount of airport tax—*redevance de développement des infrastructures aéroportuaires* (RDIA)—collected, deposited in the escrow account, and used for the repayment of the loan financing the construction of the new airport.

MEFP Table 1. Senegal: Quantitative Assessment Criteria (Performance Criteria) and Indicative Target for 2008–09 1/
(Billions of CFA francs, unless otherwise specified)

| | December 31, 2008 | | March 31, 2009 | June 30, 2009 | September 30, 2009 | December 31, 2009 |
|--|-------------------|-------|-------------------|------------------|-----------------------|----------------------|
| | Existing | | Proposed | | | |
| Assessment criteria | | | | | | |
| Floor on the basic fiscal balance 2/ | -95 | -21 | 2 | 5 | 7 | 10 |
| Ceiling on the contracting or guaranteeing of new nonconcessional external debt by the government 3/ 4/ | 80 6/ | 80 7/ | 80 7/ | 80 7/ | 80 7/ | 80 7/ |
| Ceiling on government domestic payment arrears (stock) 4/5/ | 0 | ... | ... | ... | ... | ... |
| Ceiling on spending undertaken outside normal and simplified procedures 4/ 8/ | ... | 0 | 0 | 0 | 0 | 0 |
| Ceiling on government external payment arrears (stock) 4/ | 0 | 0 | 0 | 0 | 0 | 0 |
| Ceiling on the amount of the float (<i>depenses liquidees non payees par le Tresor</i>) 9/ | 30 | 92 | 80 | 30 | 30 | 30 |
| Indicative target | | | | | | |
| Quarterly ceiling on the share of the value of public sector contracts signed by single tender (in percent) | 20 | 20 | 20 | 20 | 20 | 20 |

1/ Data for March and September 2009 are indicative targets, with the exception of the assessment criteria monitored on a continuous basis.

2/ Defined as total revenue minus total expenditure and net lending, excluding externally financed capital expenditure, on-lending, and HIPC and MDRI spending. Cumulative since the beginning of the year. Total revenue excludes privatization receipts and sales of mobile telephone licenses.

3/ This criterion excludes government or government-guaranteed CFAF borrowing from financial institutions within WAEMU. It also excludes external loans contracted by the airport project company (AIDB) to finance the construction of the new Dakar Airport.

4/ Monitored on a continuous basis.

5/ Discontinued as of the time of second review, since the broader AC on the budgetary float applies.

6/ This target is defined on a cumulative basis since the approval of the first program review. The ceiling was raised to CFAF 80 billion in the fourth quarter of 2008, to finance exclusively the Dakar-Diamniadio toll highway project. The CFAF 80 billion ceiling will be adjusted downward by the amount of any receipt from a privatization, a sale of a telecommunications license, or any other State asset (such as Sonatel shares) during 2008.

7/ This target is defined on a cumulative basis since the approval of the second program review. The amount of up to CFAF 80 billion is to finance exclusively the Dakar-Diamniadio toll highway project.

8/ Criterion applies from the time of the second PSI review.

9/ The budgetary float is defined as all the expenditure for which a bill has been received and recognized (*depense liquidee*) but which has not yet been paid by the treasury.

TABLE 2 OF THE MEFP: STRUCTURAL CONDITIONALITY, DECEMBER 2008-JUNE 2009

| Policy Measures | Target Date for Implementation | Macroeconomic Rationale |
|---|--------------------------------|---|
| Prior Action | | |
| 1. Ensure passage by Parliament of the 2009 Budget Law, as described in paragraph 12 of the MEFP. | December 15, 2008 | Ensure that the budget is consistent with the macroeconomic framework and resource availability. |
| 2. Adopt a decree amending the general regulations on government accounting (RGCP) to require use of only the normal and simplified procedures, and prohibiting the use of procedures of any other type, in particular Treasury advances, as described in paragraph 21 of the MEFP. | Completed on November 28, 2008 | Ensure macroeconomic stability and the transparency of budgetary procedures, while addressing one of the main causes of past budgetary slippages. |
| 3. Set out in a manual the detailed procedures for reconciling the budget, the TOFE, the Treasury accounts, the NGP, and the SIGFIP; establish this reconciliation for end-2007 and selected months in 2008, and publish the results, as described in paragraph 24 of the MEFP. | Completed on November 30, 2008 | Restore the reliability of the budget monitoring systems to facilitate fiscal policy assessment. |
| Structural Assessment Criteria | | |
| 1. Improve the budget procedure by adopting a decree to set the timetable and principal methods for compiling the budget, as described in paragraph 19 of the MEFP. | January 31, 2009 | Ensure that the budget is formulated in a way that is consistent with macroeconomic circumstances and the available resources. |
| 2. Adopt a decree specifying the system for the reopening and carryover of budgetary appropriations and commitments, as described in paragraph 22 of the MEFP. | February 28, 2009 | Improve the monitoring of budget execution and increase the observance of the one-year budget rule. |
| 3. Close the 2008 budget and accounting year by freezing and publishing the SIGFIP by April 30, 2009, as described in paragraph 23 of the MEFP. | April 30, 2009 | Ensure that the account statement allows for an accurate assessment of expenditure carryovers from one year to the next and facilitate government cash flow management. |

| Policy Measures | Target Date for Implementation | Macroeconomic Rationale |
|--|--------------------------------|---|
| Structural Benchmarks | | |
| 1. Adopt the decree implementing the new law on microfinance institutions. | January 31, 2009 | Enhance financial intermediation and provide better access to credit, putting into effect the new regulatory and prudential framework for this rapidly growing sector which provides one-tenth of all credit to the private sector. |
| 2. Conduct an external audit of all extrabudgetary commitments, based on terms of reference drawn up in consultation with IMF staff, as described in paragraph 26 of the MEFP. | March 31, 2009 | Create the basis for rejecting or regularizing extrabudgetary expenditure in a supplementary budget. |
| 3. Draft memoranda of understanding specifying the respective rights and duties of the APIX, DGID, and DDI regarding the management of the DISEZ, as stated in paragraph 30 of the MEFP. | March 31, 2009 | Safeguard government revenue. |
| 4. Compile and publish the first audit report of the Government Procurement Regulatory Authority (ARMP), as described in paragraph 28 of the MEFP. | May 31, 2009 | Increase fiscal transparency and governance. Assess the functioning of the new government procurement framework. |