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Democratic Republic of São Tomé and Príncipe: Third Review of the Three-Year Arrangement Under the Poverty Reduction and Growth Facility, and Request for Waiver of Performance Criteria, and Modification and Deletion of Performance Criteria—Staff Report; Press Release on the Executive Board Discussion; and Statement by the Executive Director for the Democratic Republic of São Tomé and Príncipe

In the context of the third review of the three-year arrangement under the Poverty Reduction and Growth Facility, and request for a waiver of performance criteria, and a modification and deletion of performance criteria, the following documents have been released and are included in this package:

- the staff report for the Third Review of the Three-Year Arrangement Under the Poverty Reduction and Growth Facility, and Request for Waiver of Performance Criteria, and Modification and Deletion of Performance Criteria prepared by a staff team of the IMF, following discussions that ended on November 17, 2006, with the officials of the Democratic Republic of São Tomé and Príncipe on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on December 28 , 2006. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF;

- a Press Release summarizing the views of the Executive Board as expressed during its January 17, 2007 discussion of the staff report that completed the review and request; and

- a statement by the Executive Director for the Democratic Republic of São Tomé and Príncipe.

The documents listed below have been or will be separately released.

Letter of Intent sent to the IMF by the authorities of São Tomé and Príncipe*
Memorandum of Economic and Financial Policies by the authorities of São Tomé and Príncipe*
Technical Memorandum of Understanding*
*Also included in the staff report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to publicationpolicy@imf.org.

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INTERNATIONAL MONETARY FUND

DEMOCRATIC REPUBLIC OF SÃO TOMÉ AND PRÍNCIPE

Third Review of the Three-Year Arrangement Under the Poverty Reduction and Growth Facility, and Request for Waiver of Performance Criteria, and Modification and Deletion of Performance Criteria

Prepared by the African Department
(In collaboration with other departments)

Approved by Jean A. P. Clément and Scott Brown

December 28, 2006

- Following completion of the second program review on a lapse-of-time basis (Country Report No. 06/400) in August, performance under the third program review has been mixed; five end-June 2006 performance criteria were missed. However, remedial actions have since brought performance broadly back to the program path. The report focuses on:

  (i) fiscal and monetary actions taken to combat inflation which accelerated early in 2006;

  (ii) progress on structural reforms, notably in public resource management, tax reform, and the environment for private sector activity; and

  (iii) the financial program for 2007 which focuses on reducing inflation and managing oil and debt relief resources efficiently to enhance propoor spending.

- In staffs' assessment, São Tomé and Príncipe has made significant progress on all HIPC completion point triggers. The completion point document is expected to be issued to the Boards of the IMF and the World Bank by end-January 2007.

- Discussions on the third review were held in São Tomé during November 4–17, 2006. The staff team comprised Mr. Kouwenaar (head), Mr. Ronci, Mr. Segura, and Ms. Takebe (all AFR). Mr. Randriamaholy (Resident Representative for São Tomé and Príncipe stationed in Gabon) and Mr. Worrell (MCM) participated in the mission. Mr. Nguema Affane, advisor to the Executive Director for São Tomé and Príncipe, attended the meetings. The mission overlapped with a World Bank mission.

- The mission met with the Governor of the Central Bank of São Tomé and Príncipe and the Ministers of Planning and Finance, Natural Resources, Education, and Labor. It was received by the President and the Prime Minister on the last day of the visit. The mission met with representatives of the National Assembly, trade unions and NGOs, the private sector, the donor community, and the media.

Contents Page

Appendices

EXECUTIVE SUMMARY

- **In 2006, growth has been solid; after accelerating, inflation has begun to recede.** The pick up in activity resulted from election-related spending (and related private inflows). Inflation has started to decelerate from its August peak of 26 percent.

- **Financial program performance was disappointing in the first half of 2006, but remedial measures have since brought it broadly back to the program path.** Fiscal measures since May have largely made up for election-related overruns and the domestic primary deficit in 2006 should be within the original target of 15½ percent of GDP. Propoor spending is likely below target.

- **To curb inflation, the Central Bank of São Tomé and Príncipe (BCSTP) has stepped up its efforts to contain liquidity growth.** It is issuing certificates of deposits and resuming its regular foreign exchange auctions. It has committed to adhere to its base money target while sterilizing foreign inflows. The exchange rate remains largely market determined.

- **The draft 2007 budget shows significant consolidation efforts, given less favorable prospects for oil bonuses and the need to increase propoor spending.** It would reduce nonessential spending, limit the wage bill increase, and implement new tax measures. Propoor spending would also be boosted by prospective HIPC relief and MDRI resources following the completion point.

- **Structural reforms are progressing.** Five of six structural benchmarks through September 2006 were met, some with delays. The authorities strengthened public financial management (PFM) (although full implementation of the new PFM system was delayed to end-2007) and laid the basis for tax reform and actions against money laundering. The 2007 agenda includes implementing a pilot PFM system and strengthening the environment for private sector activity (notably, in the energy and financial sectors).

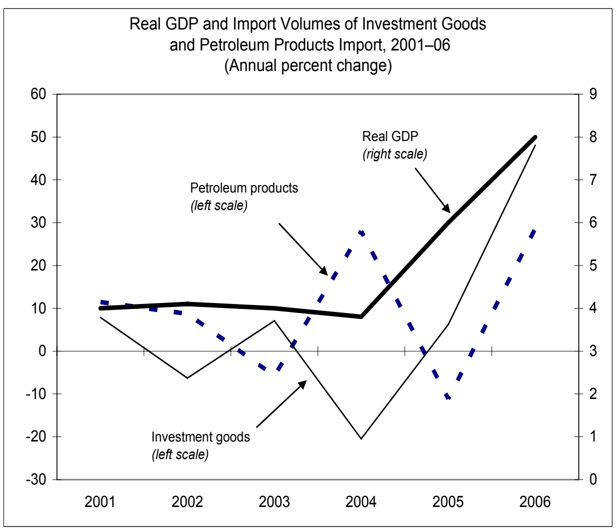
- **Risks to the program are important but seem manageable.** The increase in propoor spending depends partly on reducing nonpriority spending but should be helped by strict monitoring of budget execution using a pilot PFM system. The successful reduction in inflation also depends on improved effectiveness of monetary instruments. If prospects for oil resources are less favorable, it will be necessary to quickly revise the medium-term fiscal and external borrowing strategies, starting with stronger fiscal adjustment.

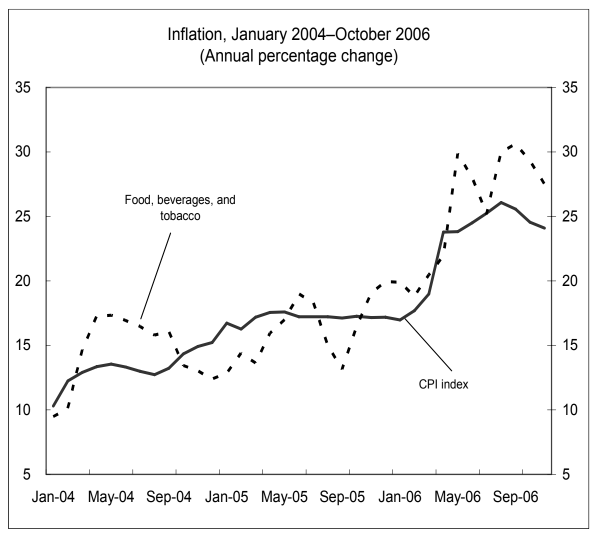
- **Staff recommends completion of the review**. It supports the authorities' request for waivers for five missed performance criteria (PCs) for end-June because strong remedial actions taken since mid-year are having a favorable impact on financial aggregates and overall program performance is now broadly satisfactory. It also supports the authorities' request for modification of PCs for end-December 2006 because, despite the remedial actions, the election-related spending and somewhat higher inflation have not allowed a full return to the original nominal program targets.

I. BACKGROUND

1. **The main goals of São Tomé and Príncipe are to achieve the HIPC completion point early in 2007 and successfully bridge the transition to the oil era.** Discussions with the authorities focused on reaching the HIPC milestone by assuring macroeconomic stability and performing well on the PRGF program. This would allow for higher propoor spending and progress toward the MDGs. Debt relief resources, combined with gradual use of oil signature bonuses, should support economic growth until oil production begins around 2012. However, further drilling is needed to confirm the existence of commercial oil reserves. The authorities agreed that building strong institutions will help ensure efficient and transparent use of debt relief and oil resources.

2. **This year's local, parliamentary, and presidential elections have strengthened democratic institutions.** President de Menezes and his coalition won all three elections. The peaceful election process and outcome have enhanced political stability, but the government still lacks a majority in the National Assembly. However, parliamentary activity has been buoyant with adoption of several critical reforms.

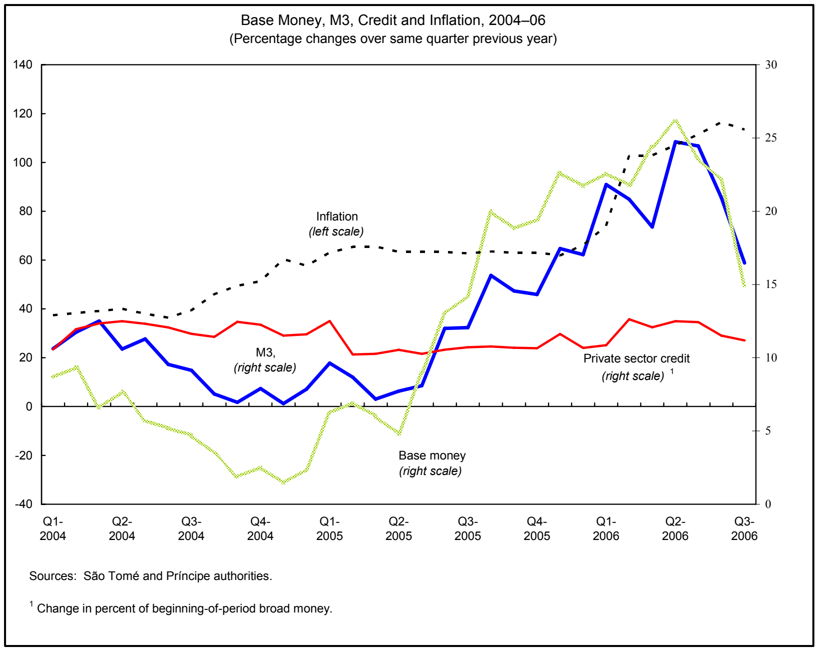




II. BROADLY SATISFACTORY PERFORMANCE AND STRENGTHENED ECONOMIC ACTIVITY

3. **Economic activity picked up in 2006 but inflation flared up temporarily**. Real GDP growth should reach 8 percent, reflecting buoyant construction activity and strong growth in services, especially tourism. The 12-month inflation rate rose from 17 percent in 2005 to 26 percent at end-August, but has since decelerated and headed down to 24 percent by November. The rise was due to both temporary exogenous factors and expansionary domestic policies (MEFP, ¶3).

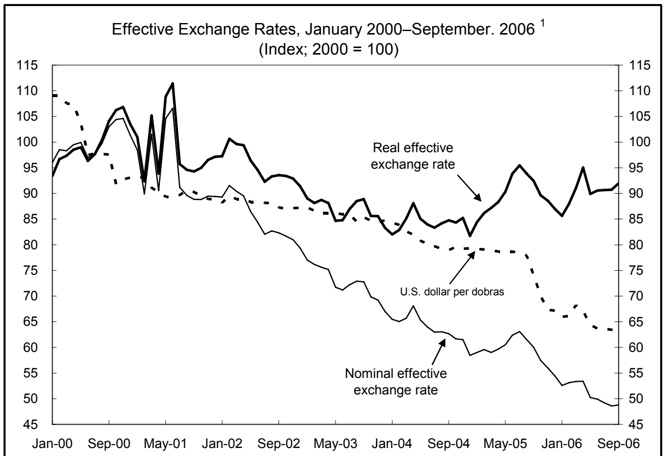
4. **Financial performance was disappointing in the first half of 2006, mainly because of expenditure overruns related to the elections and unforeseen needs** (LOI, ¶3. MEFP, ¶5). As a result, five interrelated fiscal and monetary performance criteria (PCs) for end-June were missed (Table 8), the two fiscal ones with small margins, but the three monetary ones with large margins, mainly because of delays in oil bonuses;[1] correcting for these delays, the monetary PCs are missed with a small margin.



5. **The fiscal overruns and insufficient monetary policy response to private capital inflows led to higher money growth and inflation than was programmed.** The main sources of money growth were the unexpected expansion of net credit to government, the tendency of the BCSTP to overshoot the NIR targets,[2] and large unsterilized private capital inflows, which partly translated into foreign currency deposits and strong growth in private sector credit (MEFP, ¶¶6–7). As inflation rose, the BCSTP raised its reference interest rate from 18.2 percent to 24 percent in May and to 28 percent in September and slightly increased reserve requirements, but with virtually no impact on liquidity. Concern about NIR levels as well as exchange rate depreciation also led the BCSTP to suspend its foreign exchange auctions and revert to direct sales, while rationing foreign exchange to commercial banks based on demand from priority sectors.

[1] As described in Country Report No. 06/400, page 11, an adjustor to correct for higher or lower than expected oil bonuses applies to these performance criteria for the quarterly targets from September 2006.

[2] The BCSTP overshot most NIR targets since mid-2005, except at end-June 2006. This is because the NIR target for this test date (3rd review) was set in flow terms since the beginning of the year, at the time when the overshooting on NIR at end-2005 was not yet known (Country Report No. 06/349).



Source: Information Notice System.
[1] An increase in the index corresponds to an appreciation of the effective exchange rate.

6. **The exchange rate, nevertheless, continues to be largely market determined.** The informal market premium has stayed small and commercial bank exchange rates have stayed close to the BCSTP rates for two reasons: (i) the dominant bank has managed sales to meet client demand by adjusting its rate; (ii) the BCSTP adjusts its reference rate daily, using a weighted average of its own rate (60 percent) and the average commercial bank rate (40 percent) of the previous day. In the 12 months through November, the Dobra depreciated against the U.S. dollar by 10 percent in nominal terms and appreciated in real teams. The real appreciation reflected in part the private capital inflows during the election period.

7. **Financial performance has improved since mid-year as several measures were implemented to return to the program path for 2006, but propoor spending is still below expectations** (MEFP, ¶¶12–13). The collection of tax arrears and containment of expenditure especially should make it possible to reach the original domestic primary deficit target (15½ percent of GDP). In addition, the government has taken new tax measures which will have an impact in 2007, notably the increase in excises on services from 5 to 7 percent (a measure delayed from May) and on imported alcohol and tobacco. At the same time, the growth of monetary aggregates has slowed significantly since mid-year; 12-month growth of base money fell to below 35 percent at end-November (from over 100 percent at end-June).

8. **Despite these strong efforts, the higher-than-planned election spending and higher inflation in 2006 allow only a less-than-full return to the original financial targets for year-end.** The level of the domestic primary deficit is expected to be slightly above the program target in 2006, requiring also somewhat higher bank financing. While 12-month inflation and base money growth have been falling every month since August, inflation is projected at 25 percent at end-2006, still above the program target. Therefore, the revised program for 2006 proposes to slightly modify the four quantitative PCs at end-December 2006 (Table 8; and ¶26 below).

9. **Structural reforms are progressing well and five of the six benchmarks through September were met, though some with short delays** (MEFP, ¶¶8–9 and Table 4).

- The country made good progress toward a new public financial management system (SAFE) by preparing the organic public finance law, a new budget classification in line with international standards (a prior action), and a pilot SAFE for 2007 (Box 1).

However, the original target of fully implementing the SAFE by end-2006 (a structural PC for the fourth review) will not be met because agreement with a key donor and technical preparation took longer than expected. The authorities intend to implement the SAFE by end-2007 and a new structural PC will be proposed in due course for the sixth program review (LOI, ¶3; MEFP, ¶37 and Table 2).

- Reform of the regulatory framework for private sector activity progressed, ahead of schedule, in the last quarter of 2006: (i) adoption by the National Assembly (NA) of new customs codes and regulations; (ii) submission to the NA of six draft laws on tax administration procedures and direct taxation, as well as the draft new investment code (which provides equal treatment for domestic and foreign investors); (iii) submission to the NA of the draft anti-money laundering law; and (iv) promulgation of the law on arbitration tribunals.

III. Policy Framework through end-2007

10. **Policies for 2007 are designed to consolidate macroeconomic stability and ensure sound management of oil-related and debt relief resources** (MEFP, ¶20). Staff considers the envisaged reduction in inflation to within 10–15 percent to be achievable because of the fiscal consolidation and monetary tightening under way since mid-2006. Also, certain one-off factors, such as election-related capital inflows and budget spending, will not be recurring. The authorities envisage prudent use of existing oil bonuses (in line with the Oil Revenue Management Law (ORML)) and significantly higher propoor spending thanks to prospective HIPC and MDRI debt relief. They are progressively putting in place their PFM system to better monitor the use of public resources.

A. Strengthening Fiscal Policy in the Context of Debt Relief and Oil Resources

11. **The draft 2007 budget[3] would reduce the domestic primary deficit (by 2½ percent of GDP), while increasing propoor spending** (MEFP, ¶21). Though ambitious, this fiscal consolidation is achievable with the measures planned. The domestic primary deficit is financed by (i) the use of existing oil bonuses equivalent to 8.5 percent of GDP (compared to 19.4 percent of GDP in 2006); and (ii) net external financing (minus debt service paid) of 4.3 percent of GDP (text table).

[3] Submission to the National Assembly of the draft 2007 budget agreed with IMF staff is a prior action.

São Tomé and Príncipe: Financing of the Domestic Primary Balance (Percent of GDP)			
	2005	2006 Est.	2007 Proj.
Domestic non–oil revenue	**25.8**	**30.1**	**29.2**
Domestic primary spending	**41.8**	**45.4**	**42.2**
Of which: propoor	9.2	9.7	13.8
Wages	13.5	13.5	12.8
Non–wage recurrent primary spending and net lending	21.9	25.3	20.4
Of which: elections plus extra–budgetary spending	0.0	3.6	0.0
Domestically financed capital spending plus HIPC spending	6.4	6.6	9.0
Domestic primary balance	**-15.9**	**-15.3**	**-12.9**
Financing	**15.9**	**15.3**	**12.9**
Use of oil resources for budget	21.3	19.4	8.5
Net external financing (including program support and debt relief)	-5.2	-4.4	4.3
Domestic financing (including interest payments)	-0.2	0.3	0.2
Memorandum Items			
Foreign financed capital spending	21.7	23.7	19.5
Of which: propoor	16.0	13.6	12.2
Total propoor spending (including from HIPC/MDRI resources)	25.2	23.3	26.0

Sources: São Tomé and Príncipe authorities, and IMF Staff estimates and projections.

12. **After rising significantly in 2006, the revenue-to-GDP ratio would decline slightly in 2007.** The projected full-year impact of increases in excises and other revenue measures adopted in 2006 would be partly offset by lower collection relative to GDP of fuel and import taxes as international oil prices decline and the real exchange rate appreciates modestly.

13. **In 2007, the authorities intend to initiate major tax reforms aimed at improving incentives, reducing distortions, lowering certain rates, and enlarging the tax base:**

- **Direct taxation** (MEFP, ¶19; Box 2)**.** It is expected that the new tax administration and direct tax laws will be adopted in the first quarter of 2007, with the new tax procedures implemented during 2007 and the direct tax laws applying from 2008.

- **Petroleum taxation** (MEFP, ¶12)**.** The pricing and tax structure to be adopted by mid-March 2007 should ensure that tax revenue is more stable and pump prices closely follow world prices. The current structure makes tax revenue and margins of the majority state-owned wholesaler (ENCO) and retailers volatile and leads to losses in distribution and to subsidies across products. The reform would partly move to specific taxes and margins in U.S. dollar cents per liter, and bring tax rates more in line with international practice. By providing realistic distribution margins, it would also help ENCO clear its tax arrears.

- **Indirect taxation** (MEFP, ¶27). Besides implementing the new customs codes, the authorities intend to undertake, with external support, a comprehensive review of indirect taxation, starting with a study during 2007 of ways to enlarge the tax base, including the informal sector, and move to a general sales tax.

14. **Containing wages and reducing nonwage nonessential spending would create space for more propoor spending** (MEFP, ¶21). The fiscal program envisages:

- a 20 percent increase in the government wage bill, including a general wage increase of about 18 percent and some social sector hiring;[4]
- a reduction in nonwage nonessential spending from 25 to 20 percent of GDP with lower discretionary spending in real terms (Text Table). The first phase of SAFE should help keep spending strictly in line with budget allocations (MEFP, ¶25 and structural benchmarks in Table 2; Box 1); and
- a significant increase in propoor spending, from 23 to 26 percent of GDP, reflecting the increased prospective HIPC and MDRI flow relief (MEFP ¶21).

15. **The authorities are committed to further enhancing the transparency of oil revenue management** (MEFP, ¶¶21, 26). The drilling results needed to confirm that oil reserves are commercially viable may not be available until late in 2007. The delay introduces uncertainty about the start of oil production (expected for 2012) and the receipt of further signature bonuses (for already licensed and new blocks) and complicates medium-term fiscal management. Conscious of these risks, the authorities and the National Assembly have reiterated their wish to manage oil resources prudently and transparently in the context of the ORML and the Extractive Industries Transparency Initiative (EITI). The staff welcomed the steps being undertaken to implement—with World Bank support—both the ORML (publishing the ORML handbook and putting the Petroleum Oversight Committee in place) and the EITI (notably creating a national stakeholder committee); it advised the authorities to integrate where possible any overlapping requirements for oversight.

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[4] With this general increase, real wages of government workers would return broadly to their level in 2004.

Box 1. Public Financial Management Reform

The reform aims to put in place a fully integrated computerized budget preparation and execution system (SAFE) by end-2007 for the 2008 budget. The reform is supported by the World Bank and will benefit from a software system to be provided by the Government of Angola.

Legal framework. As a first step, a new organic budget law was submitted to the National Assembly in late 2006 to modernize budget preparation and execution, and allow budget procedures to be anchored in the new system. At the same time, the government adopted new budget classifications which are consistent with the *Classification of the Functions of Government (COFOG)* for functional classification and the *Government Finance Statistics Manual 2001* for economic classification.

Comprehensiveness. SAFE will incorporate modules on treasury management, planning and patrimony, and public accounts. It will be matched by a new procurement law and procedures. It will allow decentralized budget execution by ministries and autonomous entities.

Phasing in. The government is preparing a pilot version (SAFINHO) which will be used for the 2007 budget. The pilot will link the departments of budget, treasury and revenues in a single network that will unify preparation and execution of the budget. SAFINHO will give the Ministry of Planning and Finance experience with the system while the other elements are put in place.

Classification issues. Preparation of the 2007 budget with the new classification will require: (i) consistency with the old classification of accounts, used in the *Tabela das Operações Financeiras do Estado* (TOFE) and for the fiscal program targets; and (ii) identifying propoor expenditure for tracking.

B. Monetary and Exchange Rate Policies

16. To reduce inflation to 10–15 percent in 2007, the BCSTP intends to tighten monetary policy, while sticking to its base money target (MEFP, ¶¶14–15). The monetary tightening initiated in the second half of 2006 should bring 12-month base money growth down to 28 percent in 2006 (from 50 percent at end-September 2006) and further down to 21½ percent in 2007. The BCSTP plans to do this mainly by the sale of foreign exchange and the issuance of central bank CDs.

17. **The BCSTP is resuming its regular foreign exchange auctions and continuing direct sales for specific uses, while meeting its NIR target and avoiding excessive exchange rate fluctuations** (MEFP, ¶16). The amounts to be offered at the Dutch, single-

price auctions will be based on forecast foreign exchange flows, government use of oil bonuses and foreign aid, and the NIR target.[5] Because the sales to meet needs of the national fuel importing company (ENCO) could distort the auction, they will be conducted directly with banks on request, at the BCSTP reference rate. In the intervals between auctions, the BCSTP will continue to set its reference rate as a weighted average of its own and the commercial bank exchange rates of the previous day.

18. **The auction procedures have recently been revised to enhance the transparency and market responsiveness of exchange rate determination and pave the way for adoption of Article VIII (Sections 2(a), 3, and 4) obligations** (MEFP, ¶¶16, 29). After the elimination in early 2006 of the multiple currency practice related to the spread between BCSTP buying and selling rates (the spread was set at 2 percent), the authorities will remove the exchange restriction on transfers abroad of dividends with the new Investment Code (adoption expected by end-2006). The remaining exchange restriction and multiple currency practice arise from the possibility of BCSTP rationing at the auctions and of commercial bank rates deviating temporarily by more than 2 percent from the BCSTP reference rate between auctions.[6] The combination of regular auctions and daily adjustment of the BCSTP rate should, however, soon enable São Tomé and Príncipe to adopt Article VIII status.

19. **The BCSTP intends to strengthen its financial position, enhance the transparency of its operations, and scale down the cost of a new building** (MEFP, ¶18). The financial position of the BCSTP is weak despite high levels of NIR. A joint government-BCSTP commission is examining ways to significantly reduce the contracted cost of the building (US$8 million, of which $2.4 million has already been paid).[7]

C. Improving the Climate for Private Sector Development

20. **Private sector development should benefit in 2007 from structural reforms covering taxation, the business climate, the energy sector, and banking supervision.** The program includes two structural benchmarks and a performance criterion on energy and banking sector reform measures (MEFP, Table 2).

21. **The authorities intend to implement the Investment Code in June 2007 and new tax administrative codes and new customs codes in 2007; draft a new labor code in 2007; and implement a direct tax reform from 2008** (Box 2; MEFP, Table 3).

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[5] Under current regulations, the BCSTP reserves itself the right to set the exchange rate resulting from the auction rate below the market clearing rate, and ration all bidders proportionally.

[6] Based on information available to staff (see ¶6 above), the suspension of the auctions did not result in an intensification of this exchange restriction or multiple currency practice.

[7] Because of the contract, key BCSTP board members were suspended in May 2006 (Country Report No. 06/400).

Box 2. Tax Reform

São Tomé and Príncipe is bringing its tax legislation in line with international standards. Several draft tax codes are before the National Assembly for approval between late 2006 and end-March 2007, and for implementation during 2007 and early 2008.

The new Investment Code calls for equal treatment of foreign and domestic investors, guarantees unrestricted repatriation of capital gains and profits, and sets the general conditions for tax exemption regimes, which must be stipulated in tax legislation.

The General Tax Code and Tax Procedural Code modernize tax administration procedures and create specialized courts for resolving appeals and enforcing collections. The latter is critical as under current legislation the tax authorities have few instruments to fight tax evasion. The codes are to become effective within 90 days of their approval.

The draft corporate and personal income tax codes seek to harmonize taxation between enterprises and individuals, improve the rate structure, and strengthen tax assessment. The drafts have benefited from technical assistance from the IMF. Bringing corporate tax rates down from the current 40–45 percent would align them with international levels. The draft personal income tax code applies one tax to all forms of income (not just salary, as is the case today) and introduces progressivity. How different tax rates would affect revenue is still being studied, in consultation with IMF staff. Both codes are expected to be voted early in 2007 and become effective in 2008.

Draft laws for inheritance tax and urban real estate tax aim to make collection more efficient.

The objective of **the Customs Code and related regulations** is to unify dispersed regulations and give customs adequate tools for assessing import values. Customs procedures will be updated and alternative valuation methods considered for gradual application as customs administration capacity grows.

22. **The authorities are aware that restructuring of the electricity and water sector is urgent because insufficient and erratic production and financial losses have high costs to the budget and the economy.** The state-owned electricity company (EMAE) has high costs and suffers major leakages in distribution and billing.[8] The financial loss in 2006 is almost 3 percent of GDP and debt rose to 18 percent of GDP in October 2006 (including significant arrears to domestic suppliers, such as ENCO). Although EMAE's turnover represents 8 percent of GDP, it pays little or no taxes on imported fuel or electricity sales. To address the situation, the authorities in late 2006 adopted a strategy for the sector, aimed at

[8] Just over one-half of electricity production and two-fifths of water production generate revenue; the rest is lost in distribution, unbilled consumption, and unpaid bills.

eliminating EMAE losses over the next two years.[9] The plan includes greater reliance on hydropower, purchase contracts with Independent Power Producers (IPP), and the continuing introduction of prepaid electricity meters.

23. **The authorities and staff agree on the need for better supervision of banks, especially since the banking system has expanded rapidly in recent years and there is a risk of money laundering** (MEFP, ¶28 and Table 5). The new licensing regulations must be strictly applied and minimum capital requirements increased. In recent years, with high bank liquidity and many new banks, rapid credit growth has been accompanied by a deterioration in financial indicators like loan portfolio quality (Table 12). While the BCSTP has recently stepped up its on- and off-site inspections, it needs to issue further prudential regulations, notably on credit classification, liquidity, transactions with related parties, and limits on banks' net open foreign currency positions. Finally, after the anti-money laundering law is adopted, the BCSTP plans to operationalize the Central Risk Unit and implement "know-your-client" rules for banks.

D. Donor and Debt Issues

24. **The 2007 program is fully financed through identified project support and budget support from two key partners** (MEFP ¶¶22, 33). In December 2006, the government hosted a Round Table to seek further donor support, which will likely be through projects. In line with the appraisal in the first PRSP Annual Progress Report, the authorities are aware that increased donor support requires them to improve the quality of propoor spending and strengthen PFM.

25. **The staff assessment is that São Tomé and Príncipe has made significant progress on all the HIPC completion point triggers established in December 2000 (MEFP, ¶¶30).** In preparation for the completion point, the authorities are now concluding bilateral agreements under the September 2005 Paris Club terms of reference, and continue seeking comparable treatment from non-Paris Club bilateral creditors.

IV. Program Monitoring and Risks

26. **Completion of the fourth program review is conditional on observance of the end-December 2006 performance criteria (PCs)** (LOI, ¶3; MEFP, ¶¶35–37 and Tables 1–2). The authorities request modification of the targets for four quantitative PCs and deletion of one PC for end-December 2006. Staff supports this request because the elections and delays in oil bonus receipts have complicated financial management in 2006; with

[9] The World Bank is helping the authorities devise a strategy for reform of public enterprises, including EMAE, as part of PEMFAR (Public Expenditure Review, Public Finance Management Review and Procurement Review).

inflation now higher, a full return to the original nominal targets for end-year is out of reach. The authorities propose deletion of one structural PC for end-December 2006 and establishment of a new structural PC for end-March 2007. The authorities are further strengthening their program monitoring and technical capacity with IMF and World Bank staff support.

27. **The risks to program implementation seem manageable.** First, the fiscal program and increase in propoor spending rely on containing nonessential spending and the wage bill increase; this will require firm policy commitment and application of budget procedures. Second, the reduction in inflation relies—in addition to fiscal restraint—on proactive use by the BCSTP of its monetary instruments and liquidity forecast, which may pose challenges. Third, prospects of oil could become less favorable if there are no production sharing contracts for already licensed blocks or no further licensing rounds; in that case the authorities would need to quickly adjust their medium-term fiscal and external borrowing strategies, including greater reliance on concessional borrowing.

V. Staff Appraisal

28. **Though performance was disappointing in the first half of 2006 (election-related fiscal slippage, weak monetary policies, rising inflation), remedial actions brought the program broadly back to its original path later in the year, and progress in structural reforms was strong.** Overall performance has been satisfactory, for three main reasons:

- Since May, the government has implemented measures to offset the slippage, bringing the fiscal outcome through September and the outlook for the year broadly in line with the program. However, propoor spending has been below target.

- The BCSTP has responded (though slowly) to the excess liquidity by a more effective use of its monetary instruments. Money growth and inflation have started to decline.

- The authorities made significant progress toward strengthening public financial management (PFM), the tax system, and the environment for private sector activity in 2006, and laid the basis for fuller reforms in 2007–08.

29. **The program for 2007 is ambitious but achievable in terms of inflation (10–15 percent) and fiscal effort (2½ percent of GDP) and would use oil bonuses prudently and increase propoor spending.** These objectives are supported by structural measures to improve PEM and implement tax reform. Three areas are critical for success:

- **To create space for propoor spending, nonessential spending and wage outlays must be held within budget allocations**. The authorities need to vigorously implement the new PFM system, apply the new classification, and track all spending, whether or not financed by debt relief.

- **To reduce inflation, the base money and NIR targets must be adhered to.** The BCSTP needs to move promptly to mop up liquidity as needed to sterilize foreign inflows or budgetary use of oil bonuses. The recent resumption of foreign exchange auctions and issuance of CDs are encouraging.

- **To further enhance the market responsiveness of exchange rate determination, regular foreign exchange auctions should be held.** This should help pave the way for the authorities to adopt, in due course, the Article VIII obligations.

30. **Other structural reforms are well focused on improving the environment for private sector activity and broad-based growth.** The authorities are encouraged to:

- Pursue adoption and implementation of the new tax and investment codes, so as to improve efficiency and give the private sector adequate incentives.

- Persevere with enhancing transparency of oil revenue management.

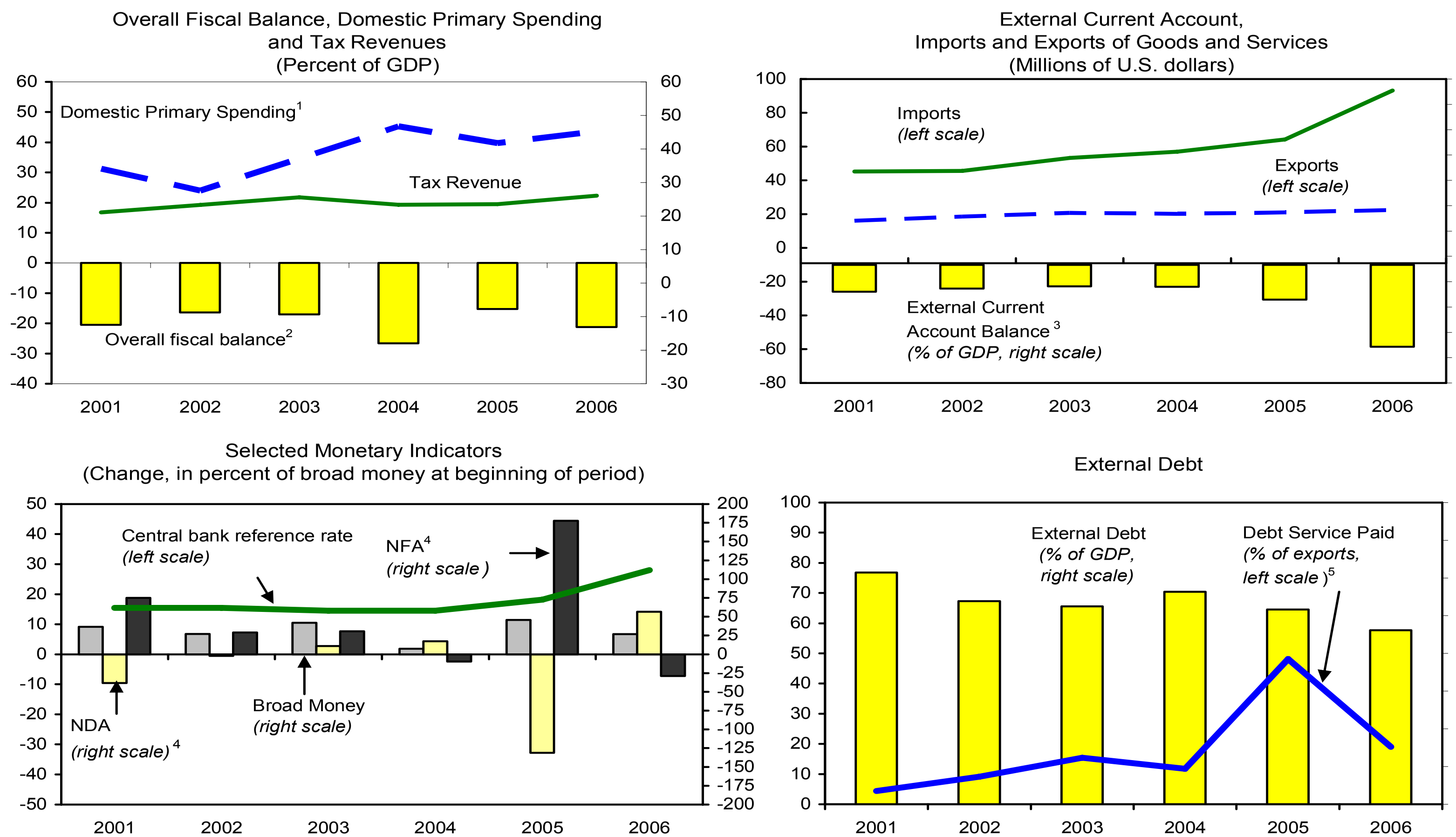
- Accelerate restructuring of the energy and water sector, so as to improve service and reduce the large losses to the budget and the economy.

- Enforce existing and issue new prudential regulations and implement the anti-money laundering law once it is adopted, so that the financial sector can contribute more to growth.

31. **Risks to the program are important but seem manageable.** There are risks related to the authorities' ability to create space for propoor spending, actively use monetary instruments to combat inflation, and promptly adjust their fiscal and external borrowing strategies should prospects for oil worsen.

32. **Staff therefore recommends completion of the third review** and approval of waivers for the nonobservance of end-June 2006 performance criteria and the modification and deletion of certain end-December 2006 performance criteria.

Fig. 1. São Tomé and Príncipe: Economic and Fiscal Indicators, 2001–06



Sources: São Tomé and Príncipe authorities, and IMF staff estimates and projections.

[1] Excluding interest payments and foreign-financed capital expenditures.

[2] Excluding oil signature bonuses and interest from NOA from 2005 onwards.

[3] In 2006, the external current account deficit is higher because of large investment-related imports in the oil and tourism sectors, financed with FDI.

[4] Includes government deposits in the National Oil Account at the BCSTP arising from oil signature bonuses.

[5] Includes payments of arrears.

Table 1. São Tomé and Príncipe: Selected Economic Indicators, 2003–10

	2003	2004	2005	2006		2007	2008	2009	2010
				CR/06/400	Revised Prog.	Prog.		Proj.	
				(Annual percentage changes, unless otherwise specified)					
National income and prices									
GDP at constant prices	4.0	3.8	6.0	5.5	8.0	7.0	7.0	7.5	8.0
GDP deflator (percentage change)	9.2	9.7	14.7	17.2	19.0	19.8	10.9	8.8	6.7
Consumer prices (percentage change; end of period)	10.2	15.2	17.2	22.0	25.0	13.5	9.5	7.0	6.0
Consumer prices (percentage change; average)	9.6	12.8	16.3	19.8	21.4	18.6	11.4	8.2	6.5
External trade									
Exports, f.o.b.	29.4	-45.5	-6.4	-4.6	-4.6	3.3	5.0	4.0	0.7
Of which : cocoa	34.9	-47.2	-7.4	-6.2	0.5	-3.6	1.3	0.6	0.0
Imports, c.i.f.	18.1	7.1	15.7	42.7	51.9	9.6	8.5	8.2	8.7
Exchange rate (dobras per U.S. dollar; end of period) [1]	9,456	10,104	11,996	…	13,139	…	…	…	…
Real effective exchange rate (depreciation -)	-2.0	-2.0	10.4	…	…	…	…	…	…
Terms of trade	9.1	-26.5	-12.0	-5.1	-4.8	3.2	0.9	0.7	0.2
Money and credit (end of period)									
Net foreign assets [2, 3]	30.8	-9.8	177.8	94.5	-29.0	35.7	66.2	5.2	3.5
Net domestic assets [2, 3]	11.0	17.1	-131.9	-74.9	58.4	-10.4	-47.5	10.2	9.7
Of which: credit to government (net) [2, 3]	15.3	6.0	-97.9	-61.5	42.8	-15.9	-52.6	13.3	9.7
credit to the economy [2]	20.6	34.4	21.2	12.6	14.9	12.6	10.0	9.0	8.3
Broad money	41.8	7.4	45.9	19.6	29.4	25.3	18.7	15.4	13.3
Velocity (GDP to average broad money ratio)	2.3	2.2	2.1	2.0	2.0	…	…	…	…
Central bank reference interest rate (percent; end of period) [1]	14.5	14.5	18.2	24.0	28.0	…	…	…	…
Commercial bank lending rate (percent; end of period)	30.0	30.0	32.5	…	…	…	…	…	…
Commercial bank deposit rate (percent; end of period)	10.3	10.3	12.8	…	…	…	…	…	…
				(Percent of GDP, unless otherwise specified)					
National accounts									
Consumption	119.0	122.0	126.2	124.9	125.6	122.2	123.3	122.5	121.0
Gross investment	36.1	35.2	34.1	67.6	63.9	64.0	65.1	64.7	65.4
Public investment	20.1	20.1	13.4	16.3	14.4	13.7	14.0	13.7	13.4
Private investment	16.0	15.1	20.7	51.3	49.4	50.3	51.1	51.0	52.0
Of which: non-oil sector (percent of non-oil GDP)	16.1	15.1	15.1	25.6	25.6	29.5	30.0	30.0	31.0
Gross domestic savings	-19.0	-22.0	-26.2	-19.9	-25.6	-22.2	-23.3	-22.5	-21.0
Public savings (excluding oil bonuses)	-1.8	-13.3	-4.2	-6.3	-6.3	-4.0	-3.1	-1.1	0.2
Gross national savings	13.4	12.1	3.3	4.4	5.3	2.4	1.8	1.5	1.9
Government finance									
Total revenue, grants and oil signature bonus	58.1	60.6	127.2	104.1	54.6	262.4	76.5	49.2	48.5
Of which : tax revenue	20.7	23.4	23.5	27.1	26.1	25.1	25.1	25.1	25.3
grants [4, 5]	32.5	32.2	26.7	31.8	22.6	201.4	19.0	18.6	18.1
oil proceeds (signature bonuses and interest) [6]	0.0	0.0	73.4	40.1	0.8	30.8	27.5	0.7	0.6
Total expenditure and net lending	75.1	87.2	69.1	77.9	75.0	65.4	63.4	60.9	58.3
Of which: noninterest current expenditure	28.4	41.7	36.7	39.1	39.8	34.1	32.1	30.5	28.7
capital and HIPC expenditures	41.9	42.1	28.0	34.1	30.2	28.5	29.1	28.5	27.9
Domestic primary balance (commitment basis; incl. HIPC Initiative spending) [7]	-11.7	-20.6	-15.9	-15.5	-15.3	-12.9	-11.9	-10.2	-8.3
Overall balance (commitment basis; including grants) [5]	-17.0	-26.6	58.1	26.2	-20.4	197.0	13.1	-11.7	-9.8
Of which: excluding oil signature bonuses and interest from NOA	-17.0	-26.6	-15.3	-13.9	-21.2	166.1	-14.4	-12.5	-10.3
Overall balance (cash basis; including grants) [5]	-11.9	-20.1	40.6	22.0	-19.2	197.0	13.1	-11.7	-9.8
External sector									
Current account balance (including official transfers)	-22.7	-23.1	-30.7	-63.2	-58.6	-61.6	-63.4	-63.1	-63.4
Current account balance (excluding official transfers)	-56.7	-58.8	-62.3	-93.9	-91.0	-86.5	-87.7	-86.6	-85.9
Net present value of total external debt after enhanced HIPC debt relief [5, 8]	…	…	1,156.4	…	1,145.3	302.6	293.4	280.3	267.0
Net present value of total external debt after enhanced HIPC and MDRI debt relief [5, 8]	…	…	933.0	…	889.7	97.0	100.9	100.5	99.3
Net present value of total external debt after enhanced HIPC and MDRI debt relief [5, 9]	…	…	1,135.8	…	861.5	89.3	90.5	86.5	81.6
Scheduled external debt service before HIPC and MDRI debt relief [10, 11]	50.3	52.3	57.2	70.2	40.1	38.3	38.5	38.2	37.3
External debt service after HIPC and MDRI debt relief [10, 11]	…	15.4	48.1	19.4	19.0	5.9	5.3	4.9	4.5
Export of goods and services (millions of U.S. dollars)	20.7	20.2	21.0	22.5	22.5	23.9	25.5	27.3	29.0
Gross foreign reserves (months of following year's imports of goods and nonfactor services) [12]	4.8	3.4	4.1	4.2	4.4	4.4	4.3	4.4	4.6
National Oil Account (millions of U.S. dollars)	…	…	23.5	37.1	8.5	14.5	38.6	31.7	26.0
Memorandum Item									
Nominal GDP (billions of dobras)	553	629	765	926	983	1,261	1,496	1,750	2,016

Sources: São Tomé and Príncipe authorities, and IMF staff estimates and projections.

[1] For 2006, through November.

[2] Percent of broad money at beginning of period.

[3] Includes government deposits from oil signature bonuses in the National Oil Account at the BCSTP.

[4] Government revenue includes HIPC and MDRI debt relief.

[5] Assumes that the completion point under the enhanced HIPC Initiative is in the first quarter of 2007.

[6] Oil signature bonuses for Blocks 5 and 6 in JDZ, totaling US$26.1 million, originally assumed for 2006, are now projected for 2007.

[7] Excluding oil revenue, grants, interest earned, and scheduled interest payments, foreign-financed scholarships, and foreign-financed capital outlays. For 2004, it also excludes transfers to the JDA.

[8] Percent of three-year moving average of exports of goods and nonfactor services.

[9] Percent of government revenue including grants and excluding oil signature bonuses.

[10] Percent of current year exports of goods and nonfactor services.

[11] Includes payments to the IMF and settlement of arrears.

[12] Gross reserves exclude the National Oil Account and guarantee deposits placed at the BCSTP by financial institutions waiting for operating licenses; imports exclude oil sector-related imports of capital goods and services.

Table 2. São Tomé and Príncipe: Financial Operations of the Central Government, 2004–10

	2004	2005	2006						2007					2008	2009	2010
			Jan.–Jun.		Jan.–Sep.		Jan.–Dec.		Jan.–Mar.	Jan.–Jun.	Jan.–Sep.	Jan.–Dec.		Proj.		
			CR/06/349	Prel. Est.	CR/06/400	Prel. Est.	CR/06/400	Rev. prog.	Prog.	Prog.	Prog.	CR/06/400	Prog.			
							(Billions of dobras)									
Total revenue and grants	**381.2**	**973.3**	**926.1**	**179.9**	**771.5**	**308.5**	**964.7**	**537.1**	**497.1**	**2,921.0**	**3,080.7**	**3,472.5**	**3,307.6**	**1,144.2**	**859.8**	**978.2**
Total revenue	178.7	207.4	124.7	146.4	215.4	227.7	298.0	306.7	54.6	163.7	265.0	361.8	380.0	447.7	521.0	602.4
Tax revenue	147.3	180.0	106.9	120.6	173.6	182.9	250.8	256.4	47.9	142.6	217.9	297.6	316.3	374.8	439.0	508.9
Of which: fuel taxes	29.8	38.2	28.0	…	44.2	…	64.2	70.0	…	…	…	…	80.0	…	…	…
Nontax revenue	31.3	27.4	17.9	25.7	41.8	44.7	47.1	50.3	6.7	21.1	47.1	64.2	63.7	72.9	82.0	93.5
Grants [1, 2]	202.6	204.4	111.2	29.0	186.7	75.0	294.9	222.1	58.5	2,371.8	2,428.6	2,721.1	2,539.1	284.9	325.9	364.7
Project grants	146.0	151.8	97.6	0.8	135.9	28.2	180.4	177.4	26.6	73.0	109.0	225.1	219.4	262.1	301.8	339.6
Nonproject grants	20.4	17.5	2.5	2.4	8.9	7.6	21.4	2.4	0.0	0.0	20.9	21.5	20.9	22.8	24.1	25.2
HIPC Initiative-related grants	36.1	35.1	11.2	25.8	41.9	39.2	93.1	42.3	31.9	2,298.8	2,298.8	2,474.5	2,298.8	0.0	0.0	0.0
Of which: multilateral HIPC relief	36.1	35.1	11.2	25.8	38.6	39.2	51.4	42.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Of which: MDRI debt relief [2]	0.0	0.0	…	0.0	0.0	0.0	31.7	0.0	31.9	2,298.8	2,298.8	2,431.2	2,298.8	0.0	0.0	0.0
Oil signature bonuses (including interest income) [3]	…	561.5	690.1	4.5	369.4	5.8	371.8	8.2	384.1	385.5	387.0	389.6	388.5	411.5	12.9	11.1
Total expenditure and net lending	**548.6**	**528.7**	**340.0**	**297.6**	**543.1**	**431.7**	**722.1**	**737.6**	**138.2**	**365.1**	**550.8**	**823.6**	**824.4**	**947.6**	**1,064.8**	**1,175.6**
Current expenditure	292.5	314.4	190.4	237.8	312.1	325.4	406.5	439.6	92.9	237.8	349.3	443.7	465.1	511.8	566.1	612.4
Personnel costs	75.7	103.2	56.8	64.5	97.2	97.2	127.5	133.0	35.8	72.4	113.9	153.0	160.9	184.0	207.4	229.6
Of which: financed by HIPC relief	…	…	0.0	0.0	0.0	0.0	24.0	12.0	5.0	10.0	15.0	35.0	20.0	20.0	20.0	20.0
Goods and services	95.8	66.2	24.9	47.0	61.3	62.8	81.9	85.6	24.4	41.2	73.3	91.8	99.6	107.4	117.8	125.7
Interest on external debt due	30.1	32.3	19.5	20.9	31.1	32.9	41.4	43.6	8.2	16.5	25.3	40.9	32.5	31.2	32.8	34.0
Interest on internal debt due	0.0	1.5	1.3	4.7	1.9	4.7	2.5	4.7	1.5	1.5	2.0	2.5	2.5	0.0	0.0	0.0
Transfers	65.9	83.2	71.0	73.6	85.6	88.1	106.6	114.2	16.1	89.7	103.6	115.5	127.7	142.7	155.3	166.2
Other	25.0	28.1	17.0	27.1	35.1	39.6	46.6	58.4	6.8	16.4	31.2	40.1	42.0	46.5	52.9	57.0
Capital expenditure	234.9	186.4	131.2	41.7	200.4	78.6	260.6	261.4	35.9	94.0	151.6	283.1	279.4	333.5	389.3	448.0
Financed by the treasury	50.5	20.7	9.1	14.3	16.2	21.9	24.2	28.8	2.6	7.5	22.6	30.4	33.2	42.1	56.5	76.2
Of which : extrabudgetary spending	0.0		0.0	9.7	0.0	9.7	0.0	9.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financed by external sources [4]	184.4	165.7	122.2	27.4	184.3	56.8	236.4	232.5	33.3	86.4	129.1	252.7	246.2	291.4	332.7	371.8
Of which : Taiwan POC	…	…	…	…	…	28.2	…	…	…	…	…	…	…	…	…	…
HIPC Initiative-related social expenditure	30.1	27.9	18.4	14.7	30.6	26.7	55.0	35.6	9.4	33.4	49.8	96.8	79.8	102.3	109.4	115.2
Net lending	-9.0	0.0	0.0	3.4	0.0	1.0	0.0	1.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall fiscal balance (commitment basis)	**-167.3**	**444.6**	**586.1**	**-117.7**	**228.3**	**-123.2**	**242.6**	**-200.5**	**359.0**	**2,555.9**	**2,529.9**	**2,648.8**	**2,483.2**	**196.5**	**-205.2**	**-197.5**
Change in arrears (net; reduction -)	41.0	-134.2	-50.6	11.7	-8.4	9.8	-38.8	12.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
external arrears [5]	13.8	-52.2	-50.6	11.8	3.3	17.7	-27.1	23.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
domestic arrears	27.2	-81.9	0.0	-0.1	-11.7	-7.9	-11.7	-11.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall fiscal balance (cash basis)	**-126.3**	**310.4**	**535.5**	**-106.0**	**220.0**	**-113.4**	**203.8**	**-188.5**	**359.0**	**2,555.9**	**2,529.9**	**2,648.8**	**2,483.2**	**196.5**	**-205.2**	**-197.5**
Financing	**126.3**	**-312.9**	**-535.5**	**106.0**	**-220.0**	**113.4**	**-203.8**	**188.5**	**-359.0**	**-2,555.8**	**-2,529.9**	**-2,648.8**	**-2,483.2**	**-196.5**	**-205.2**	**-197.5**
External (net)	**99.3**	**-38.5**	**-187.6**	**-17.0**	**-3.0**	**-32.2**	**14.3**	**-13.2**	**-190.9**	**-2,448.0**	**-2,427.6**	**-2,636.8**	**-2,407.0**	**70.4**	**74.6**	**77.8**
Disbursements (projects)	38.4	13.8	24.6	26.0	48.4	26.0	56.0	55.1	6.7	13.4	20.1	27.5	26.8	29.2	31.0	32.3
Program financing (loans)	50.3	0.0	7.8	0.0	0.0	0.0	12.7	0.0	0.0	0.0	10.5	21.5	20.9	30.4	32.2	33.5
Short-term loans (net) [6]	48.9	0.0	-200.4	0.0	0.0	0.0	0.0	0.0	-200.7	-200.7	-200.7	-214.5	-200.7	0.0	0.0	0.0
Scheduled amortization (medium- and long-term) [7]	-73.2	-94.6	-60.4	-43.0	-91.6	-58.2	-122.1	-68.3	-2.9	-2,272.6	-2,275.3	-2,501.4	-2,277.9	-13.5	-14.6	-15.6
Change in arrears (principal) [5, 8]	34.9	-101.9	-105.4	0.0	10.8	0.0	-59.1	0.0	0.0	-141.6	-141.6	0.0	-141.6	0.0	0.0	0.0
Bilateral rescheduling [8]	0.0	144.1	146.2	0.0	29.4	0.0	126.8	0.0	6.0	153.5	159.5	30.2	165.4	24.3	26.1	27.6
Domestic (net)	**27.0**	**-274.4**	**-347.8**	**123.0**	**-216.9**	**145.6**	**-218.1**	**201.7**	**-168.0**	**-107.9**	**-102.3**	**-59.5**	**-76.2**	**-368.7**	**110.5**	**93.0**
Net bank credit to the government (net of valuation changes) [9]	16.6	-277.3	-347.8	124.9	-216.9	142.4	-218.1	201.7	-168.0	-107.9	-102.3	-59.5	-76.2	-368.7	110.5	93.0
Banking system credit (excluding National Oil Account) [9]	16.6	-14.1	-40.8	-61.5	-45.1	-42.7	-43.9	19.1	-91.7	-30.1	-23.0	-22.0	4.6	-1.1	-1.0	-2.3
National Oil Account	0.0	-263.2	-307.1	186.3	-171.8	185.0	-174.2	182.6	-76.3	-77.8	-79.3	-37.4	-80.8	-367.6	111.5	95.2
Nonbank financing (including earmarked funds and residual)	10.4	2.9	0.0	-1.9	0.0	3.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**47.5**	**0.0**	**101.8**	**20.1**	**26.8**
Memorandum items:																
Domestic primary balance (commitment basis) [10]	**-129.4**	**-121.9**	**-72.4**	**-98.2**	**-110.6**	**-109.6**	**-143.8**	**-150.0**	**-40.6**	**-97.0**	**-129.3**	**-165.7**	**-163.2**	**-177.3**	**-178.2**	**-167.4**
Of which: excluding transfers to the JDA	-129.4	-89.0	-33.6	-60.0	-72.0	-71.4	-105.2	-111.8	-40.6	-46.9	-79.2	-121.4	-113.1	-119.9	-114.3	-97.5
Overall balance (commitment basis, incl. grants, excl. oil bonuses) [2]	-167.3	-117.0	-104.1	-122.2	-141.1	-129.0	-129.2	-208.7	-25.1	2,170.4	2,142.9	2,259.3	2,094.7	-215.0	-217.9	-208.5
Domestic primary spending	**294.3**	**319.7**	**189.1**	**234.2**	**315.6**	**326.9**	**431.4**	**446.3**	**95.2**	**256.8**	**386.6**	**507.5**	**531.6**	**612.3**	**685.8**	**755.8**
Total HIPC debt relief (in flows)	**36.1**	**37.6**	**24.4**	**25.8**	**67.9**	**39.2**	**102.6**	**42.3**	**26.9**	**53.8**	**80.8**	**110.6**	**107.7**	**123.4**	**130.3**	**137.5**
Multilateral debt relief (Comp. Point and MDRI in flows)	**36.1**	**35.1**	**11.2**	**25.8**	**38.6**	**39.2**	**51.4**	**42.3**	**21.0**	**41.9**	**62.9**	**80.4**	**83.8**	**99.1**	**104.2**	**109.9**
Of which: MDRI in flows	...	...	...	...	...	**0.0**	**3.7**	**0.0**	**3.9**	**7.7**	**11.6**	**22.7**	**15.4**	**18.6**	**19.9**	**21.3**

Sources: São Tomé and Príncipe authorities, and IMF staff estimates and projections.

[1] Assumes HIPC completion point in the first quarter of 2007.

[2] Includes MDRI relief as a stock of debt reduction for the IMF in the first quarter and for IDA and AfDB in the second quarter of 2007.

[3] Oil signature bonuses for Blocks 5 and 6 in JDZ, totaling US$26.1 million, originally assumed for 2006, are now projected for 2007.

[4] For 2006, includes US$2 million of the social inclusion project to compensate laid-off workers from the privatization of public agricultural enterprises during the 1990s.

[5] For 2006, refers to a temporary accumulation of technical arrears with bilateral creditors, pending reconciliation of debt records.

[6] Repayment of three US$5 million loans disbursed by Nigeria in 2002–04 is assumed for 2007, upon arrival of oil signature bonuses for Blocks 2–4 in JDZ.

[7] For 2007, includes IDA and AfDB MDRI relief as a stock of debt reduction.

[8] For 2005, reflects impact of Paris Club rescheduling in the last quarter of 2005. For 2007, assumes rescheduling agreement with non-Paris Club bilateral creditors for current maturities and stock of arrears.

[9] For 2007, includes IMF MDRI relief as a stock of debt reduction.

[10] Excluding the oil revenue, grants, interest earned and scheduled interest payments, foreign-financed scholarships, and foreign-financed capital outlays. For 2004, it also excludes transfers to the JDA.

Table 3. São Tomé and Príncipe: Financial Operations of the Central Government, 2004–10

	2004	2005	2006						2007					2008	2009	2010
			Jan.–Jun.		Jan.–Sep.		Jan–Dec		Jan.–Mar.	Jan.–Jun.	Jan.–Sep.	Jan–Dec		Proj.		
			CR/06/349	Prel. Est.	CR/06/400	Prel. Est.	CR/06/400	Rev. prog.	Prog.	Prog.	Prog.	CR/06/400	Prog.			
							(Percentage of GDP)									
Total revenue and grants	**60.6**	**127.2**	**104.1**	**18.3**	**83.3**	**31.4**	**104.1**	**54.6**	**39.4**	**231.7**	**244.4**	**308.7**	**262.4**	**76.5**	**49.2**	**48.6**
Total revenue	28.4	27.1	14.0	14.9	23.2	23.2	32.2	31.2	4.3	13.0	21.0	32.2	30.1	29.9	29.8	29.9
Tax revenue	23.4	23.5	12.0	12.3	18.7	18.6	27.1	26.1	3.8	11.3	17.3	26.5	25.1	25.1	25.1	25.3
Of which: fuel taxes	4.7	5.0	3.1	…	4.8	…	6.9	7.1	…	…	…	…	6.3	…	…	…
Nontax revenue	5.0	3.6	2.0	2.6	4.5	4.5	5.1	5.1	0.5	1.7	3.7	5.7	5.0	4.9	4.7	4.6
Grants [1, 2]	32.2	26.7	12.5	2.9	20.2	7.6	31.8	22.6	4.6	188.1	192.6	241.9	201.4	19.1	18.7	18.1
Project grants	23.2	19.8	11.0	0.1	14.7	2.9	19.5	18.0	2.1	5.8	8.6	20.0	17.4	17.5	17.3	16.9
Nonproject grants	3.2	2.3	0.3	0.2	1.0	0.8	2.3	0.2	0.0	0.0	1.7	1.9	1.7	1.5	1.4	1.2
HIPC Initiative-related grants	5.7	4.6	1.3	2.6	4.5	4.0	10.0	4.3	2.5	182.3	182.3	220.0	182.3	0.0	0.0	0.0
Of which: multilateral HIPC relief	5.7	4.6	1.3	2.6	4.2	4.0	5.6	4.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Of which: MDRI debt relief [2]	0.0	0.0	…	0.0	0.0	0.0	3.4	0.0	2.5	182.3	182.3	216.1	182.3	0.0	0.0	0.0
Oil signature bonuses (including interest income) [3]	…	73.4	77.6	0.5	39.9	0.6	40.1	0.8	30.5	30.6	30.7	34.6	30.8	27.5	0.7	0.6
Total expenditure and net lending	**87.2**	**69.1**	**38.2**	**30.3**	**58.6**	**43.9**	**77.9**	**75.0**	**11.0**	**29.0**	**43.7**	**73.2**	**65.4**	**63.4**	**60.9**	**58.4**
Current expenditure	46.5	41.1	21.4	24.2	33.7	33.1	43.9	44.7	7.4	18.9	27.7	39.4	36.9	34.2	32.4	30.4
Personnel costs	12.0	13.5	6.4	6.6	10.5	9.9	13.8	13.5	2.8	5.7	9.0	13.6	12.8	12.3	11.9	11.4
Of which: financed by HIPC relief	…	…	0.0	0.0	0.0	0.0	2.6	1.2	0.4	0.8	1.2	3.1	1.6	1.3	1.1	1.0
Goods and services	15.2	8.7	2.8	4.8	6.6	6.4	8.8	8.7	1.9	3.3	5.8	8.2	7.9	7.2	6.7	6.2
Interest on external debt due	4.8	4.2	2.2	2.1	3.4	3.3	4.5	4.4	0.7	1.3	2.0	3.6	2.6	2.1	1.9	1.7
Interest on internal debt due	0.0	0.2	0.1	0.5	0.2	0.5	0.3	0.5	0.1	0.1	0.2	0.2	0.2	0.0	0.0	0.0
Transfers	10.5	10.9	8.0	7.5	9.2	9.0	11.5	11.6	1.3	7.1	8.2	10.3	10.1	9.5	8.9	8.3
Other	4.0	3.7	1.9	2.8	3.8	4.0	5.0	5.9	0.5	1.3	2.5	3.6	3.3	3.1	3.0	2.8
Capital expenditure	37.3	24.4	14.8	4.2	21.6	8.0	28.1	26.6	2.8	7.5	12.0	25.2	22.2	22.3	22.3	22.2
Financed by the treasury	8.0	2.7	1.0	1.5	1.7	2.2	2.6	2.9	0.2	0.6	1.8	2.7	2.6	2.8	3.2	3.8
Of which: extrabudgetary spending	0.0	0.0	0.0	1.0	0.0	1.0	0.0	1.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financed by external sources [4]	29.3	21.7	13.7	2.8	19.9	5.8	25.5	23.7	2.6	6.9	10.2	22.5	19.5	19.5	19.0	18.5
Of which: Taiwan POC	…	…	…	0.0	…	2.9	…	…				…	…	…	…	…
HIPC Initiative-related social expenditure	4.8	3.6	2.1	1.5	3.3	2.7	5.9	3.6	0.7	2.6	4.0	8.6	6.3	6.8	6.3	5.7
Net lending	-1.4	0.0	0.0	0.3	0.0	0.1	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall fiscal balance (commitment basis)	**-26.6**	**58.1**	**65.9**	**-12.0**	**24.6**	**-12.5**	**26.2**	**-20.4**	**28.5**	**202.7**	**200.7**	**235.5**	**197.0**	**13.1**	**-11.7**	**-9.8**
Change in arrears (net; reduction -)	6.5	-17.5	-5.7	1.2	-0.9	1.0	-4.2	1.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Of which: external arrears [5]	2.2	-6.8	-5.7	1.2	0.4	1.8	-2.9	2.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
domestic arrears	4.3	-10.7	0.0	0.0	-1.3	-0.8	-1.3	-1.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall fiscal balance (cash basis)	**-20.1**	**40.6**	**60.2**	**-10.8**	**23.7**	**-11.5**	**22.0**	**-19.2**	**28.5**	**202.7**	**200.7**	**235.5**	**197.0**	**13.1**	**-11.7**	**-9.8**
Financing	**20.1**	**-40.9**	**-60.2**	**10.8**	**-23.7**	**11.5**	**-22.0**	**19.2**	**-28.5**	**-202.7**	**-200.7**	**-235.5**	**-197.0**	**-13.1**	**11.7**	**9.8**
External (net)	**15.8**	**-5.0**	**-21.1**	**-1.7**	**-0.3**	**-3.3**	**1.5**	**-1.3**	**-15.1**	**-194.2**	**-192.6**	**-234.4**	**-190.9**	**4.7**	**4.3**	**3.9**
Disbursements (projects)	6.1	1.8	2.8	2.6	5.2	2.6	6.0	5.6	0.5	1.1	1.6	2.4	2.1	2.0	1.8	1.6
Program financing (loans)	8.0	0.0	0.9	0.0	0.0	0.0	1.4	0.0	0.0	0.0	0.8	1.9	1.7	2.0	1.8	1.7
Short-term loans (net) [6]	7.8	0.0	-22.5	0.0	0.0	0.0	0.0	0.0	-15.9	-15.9	-15.9	-19.1	-15.9	0.0	0.0	0.0
Scheduled amortization (medium- and long-term) [7]	-11.6	-12.4	-6.8	-4.4	-9.9	-5.9	-13.2	-7.0	-0.2	-180.3	-180.5	-222.4	-180.7	-0.9	-0.8	-0.8
Change in arrears (principal) [5, 8]	5.6	-13.3	-11.8	0.0	1.2	0.0	-6.4	0.0	0.0	-11.2	-11.2	0.0	-11.2	0.0	0.0	0.0
Bilateral rescheduling [8]	0.0	18.8	16.4	0.0	3.2	0.0	13.7	0.0	0.5	12.2	12.6	2.7	13.1	1.6	1.5	1.4
Domestic (net)	**4.3**	**-35.9**	**-39.1**	**12.5**	**-23.4**	**14.8**	**-23.5**	**20.5**	**-13.3**	**-8.6**	**-8.1**	**-5.3**	**-6.0**	**-24.7**	**6.3**	**4.6**
Net bank credit to the government (net of valuation changes) [9]	2.6	-36.2	-39.1	12.7	-23.4	14.5	-23.5	20.5	-13.3	-8.6	-8.1	-5.3	-6.0	-24.7	6.3	4.6
Banking system credit (excluding National Oil Account) [9]	2.6	-1.8	-4.6	-6.3	-4.9	-4.3	-4.7	1.9	-7.3	-2.4	-1.8	-2.0	0.4	-0.1	-0.1	-0.1
National Oil Account	0.0	-34.4	-34.5	19.0	-18.5	18.8	-18.8	18.6	-6.1	-6.2	-6.3	-3.3	-6.4	-24.6	6.4	4.7
Nonbank financing (including earmarked funds and residual)	1.7	0.4	0.0	-0.2	0.0	0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**4.2**	**0.0**	**6.8**	**1.1**	**1.3**
Memorandum items:																
Propoor expenditure (millions of U.S. dollars)	14.3	18.0	…	…	…	…	20.8	18.4	…	…	…	…	23.5	…	…	…
Propoor expenditure (percent of GDP)	22.2	25.2	…	…	…	…	28.4	23.3	…	…	…	…	26.0	…	…	…
Domestic primary balance (commitment basis) [10]	**-20.6**	**-15.9**	**-8.1**	**-10.0**	**-11.9**	**-11.2**	**-15.5**	**-15.3**	**-3.2**	**-7.7**	**-10.3**	**-13.0**	**-12.9**	**-11.9**	**-10.2**	**-8.3**
Of which: excluding transfers to the JDA	-20.6	-11.6	-3.8	-6.1	-7.8	-7.3	-11.4	-11.4	-3.2	-3.7	-6.3	-9.0	-9.0	-8.0	-6.5	-4.8
Overall balance (commitment basis, incl. grants, excl. oil bonuses) [2]	-26.6	-15.3	-11.7	-12.4	-15.2	-13.1	-13.9	-21.2	-2.0	172.1	170.0	200.8	166.1	-14.4	-12.5	-10.4
Domestic primary spending	**46.8**	**41.8**	**21.3**	**23.8**	**34.1**	**33.3**	**46.6**	**45.4**	**7.5**	**20.4**	**30.7**	**45.1**	**42.2**	**41.0**	**39.2**	**37.5**
Total HIPC debt relief (in flows)	**5.7**	**4.9**	**2.5**	**2.6**	**6.9**	**4.0**	**11.1**	**4.3**	**2.1**	**4.3**	**6.4**	**9.8**	**8.5**	**8.3**	**7.5**	**6.8**
Multilateral debt relief (Comp. Point and MDRI in flows)	**...**	**...**	**...**	**...**	**...**	**...**	**5.6**	**4.3**	**1.7**	**3.3**	**5.0**	**7.1**	**6.6**	**6.6**	**6.0**	**5.5**
Of which: MDRI in flows	…	…	…	…	…	…	0.4	0.0	0.3	0.6	0.9	2.0	1.2	1.2	1.1	1.1

Sources: São Tomé and Príncipe authorities, and IMF staff estimates and projections.

[1] Assumes HIPC completion point in the first quarter of 2007.

[2] Includes MDRI relief as a stock of debt reduction for the IMF in the first quarter, and for IDA and AfDB in the second quarter of 2007.

[3] Oil signature bonuses for Blocks 5 and 6 in JDZ, totaling US$26.1 million, originally assumed for 2006, are now projected for 2007.

[4] For 2006, includes US$2 million of the social inclusion project to compensate laid-off workers from the privatization of public agricultural enterprises during the 1990s.

[5] For 2006, refers to a temporary accumulation of technical arrears with bilateral creditors, pending reconciliation of debt records.

[6] Repayment of three US$5 million loans disbursed by Nigeria in 2002–04 is assumed for 2007, upon arrival of oil signature bonuses for Blocks 2–4 in JDZ.

[7] For 2007, includes IDA and AfDB MDRI relief as a stock of debt reduction.

[8] For 2005, reflects impact of Paris Club rescheduling in the last quarter of 2005. For 2007, assumes rescheduling agreement with non Paris Club bilateral creditors for current maturities and stock of arrears.

[9] For 2007, includes IMF MDRI relief as a stock of debt reduction.

[10] Excluding the oil revenue, grants, interest earned and scheduled interest payments, foreign-financed scholarships, and foreign-financed capital outlays. For 2004, it also excludes transfers to the JDA.

Table 4. São Tomé and Príncipe: Monetary Survey, 2003–07

	2003	2004	2005	2006						2007			
	Dec.	Dec	Dec.	Jun.		Sep.		Dec.		Mar.	Jun.	Sep.	Dec.
				CR/06/400	Est.	CR/06/400	Actual	CR/06/400	Rev. Prog.	Prog.			
	(Billions of dobras; end of period)												
Net foreign assets	**324.7**	**297.7**	**824.9**	**798.4**	**795.1**	**1,167.9**	**749.8**	**1,233.8**	**699.3**	**892.6**	**874.2**	**908.1**	**899.2**
Central bank [1]	235.1	189.3	597.8	549.1	561.1	894.0	563.0	947.6	504.9	692.8	668.9	697.3	683.0
Commercial banks	89.6	108.5	227.1	249.3	234.0	273.9	186.8	286.3	194.4	199.9	205.3	210.8	216.2
Net domestic assets	**-48.6**	**-1.2**	**-392.4**	**-319.9**	**-198.9**	**-693.9**	**-160.5**	**-716.4**	**-139.7**	**-291.6**	**-226.1**	**-217.4**	**-198.1**
Net domestic credit	101.0	212.6	-14.9	124.2	149.7	-202.8	184.9	-213.8	234.4	94.1	171.0	191.5	215.9
Net credit to government	19.2	35.8	-254.4	-152.2	-142.2	-498.1	-126.8	-520.6	-69.4	-235.8	-181.7	-180.6	-158.2
Of which: valuation changes	...	...	-12.9	-18.8	-12.7	-26.7	-13.2	-48.1	-16.7	1.6	-4.5	-8.9	-12.6
Claims [1]	63.1	83.6	87.8	98.1	98.7	108.8	105.8	88.6	108.5	86.9	96.8	98.3	108.9
Deposits	-43.9	-47.8	-342.2	-250.3	-241.0	-606.9	-232.6	-609.2	-177.8	-322.6	-278.5	-278.9	-267.1
Budgetary deposits	-18.5	-19.2	-22.0	-47.3	-47.2	-62.3	-55.3	-58.9	-33.5	-46.0	-34.0	-24.5	-16.4
Counterpart funds	-13.6	-18.4	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6
Foreign currency deposits	-11.8	-10.3	-297.6	-180.3	-171.1	-522.0	-154.6	-527.7	-121.7	-254.0	-221.9	-231.8	-228.1
Of which: National Oil Account	...	0.0	-276.1	-102.1	-104.0	-474.7	-106.0	-498.5	-110.9	-190.0	-196.6	-203.3	-210.1
Credit to the economy	81.8	176.8	239.5	276.4	291.9	295.3	311.7	306.8	303.8	329.9	352.8	372.1	374.1
Of which: credit in foreign currency	51.0	121.9	142.8	164.8	205.5	176.0	208.2	182.9	202.9	...	...	...	249.9
Other items (net)	-149.6	-213.8	-377.5	-444.1	-348.6	-491.1	-345.4	-502.6	-374.1	-385.7	-397.2	-408.9	-414.0
Broad money (M3)	**276.2**	**296.5**	**432.6**	**478.5**	**596.2**	**474.0**	**589.2**	**517.4**	**559.6**	**601.1**	**648.1**	**690.7**	**701.1**
Local currency	158.3	175.8	198.6	213.0	226.5	201.9	253.3	223.1	202.5	229.9	264.7	296.0	296.4
Money	147.1	159.3	180.4	191.8	204.2	182.7	226.7	202.9	185.1	207.7	238.0	265.3	267.7
Currency outside banks	56.4	60.0	72.5	66.4	81.1	69.7	80.7	83.7	89.8	85.3	91.2	96.9	110.0
Demand deposits	90.7	99.3	107.8	125.4	123.1	113.0	146.0	119.3	95.3	122.4	146.7	168.5	157.7
Time deposits	11.2	16.5	18.2	21.2	22.3	19.1	26.6	20.2	17.4	22.3	26.7	30.7	28.7
Foreign currency deposits	117.9	120.7	234.0	265.5	369.7	272.2	335.9	294.3	357.1	371.1	383.4	394.7	404.7
	(Change in percent of beginning-of-period money stock, unless otherwise specified)												
Net foreign assets	30.8	-9.8	177.8	-6.1	-6.9	79.3	-17.4	94.5	-29.0	34.5	31.3	37.3	35.7
Net domestic assets	11.0	17.1	-131.9	16.8	44.7	-69.7	53.6	-74.9	58.4	-27.1	-15.4	-13.9	-10.4
Of which: net credit to government	15.3	6.0	-97.9	23.6	25.9	-56.3	29.5	-61.5	42.8	-29.7	-20.1	-19.9	-15.9
credit to the economy	20.6	34.4	21.2	5.5	12.1	9.9	16.7	12.6	14.9	4.7	8.8	12.2	12.6
Broad money (M3)	41.8	7.4	45.9	10.6	37.8	9.6	36.2	19.6	29.4	7.4	15.8	23.4	25.3
Memorandum items:													
Velocity (ratio of GDP to average broad money)	2.3	2.2	2.1	...	2.0	...	1.9	2.0	2.0	...	...	...	2.0
Money multiplier (M3/M0)	1.7	2.5	2.1	2.0	2.3	2.0	2.2	2.0	2.1	2.1	2.1	2.1	2.1
Base money (12-month growth rate)	41.9	-24.9	76.6	103.7	116.8	27.1	49.6	20.4	27.9	5.0	16.7	12.0	21.5
Credit to the economy (12-month growth rate)	91.0	121.2	42.0	73.2	52.1	24.2	47.5	28.1	26.8	27.2	20.8	19.4	23.1
M3 (12-month growth rate)	45.7	7.4	45.9	79.9	108.4	67.9	58.8	19.6	29.4	7.0	8.7	17.2	25.3
Commercial banks' net open position (millions of U.S. dollars)	2.4	11.0	11.6	...	5.5	...	4.7	...	3.0	...	...	...	4.3

Sources: São Tomé and Príncipe authorities, and IMF staff estimates and projections.

[1] Includes MDRI assistance from the IMF as a stock of debt reduction, totaling SDR 1.6 million assumed in the first quarter of 2007.

Table 5. São Tomé and Príncipe: Summary Accounts of the Central Bank, 2003–07

	2003	2004	2005	2006						2007			
	Dec.	Dec.	Dec.	Jun.		Sep.		Dec.		Mar.	Jun.	Sep.	Dec.
				CR/06/400	Actual	CR/06/400	Actual	CR/06/400	Rev. Prog.		Prog.		
	(Billions of dobras, end of period)												
Net foreign assets	**235.1**	**189.3**	**597.8**	**549.1**	**561.1**	**894.0**	**563.0**	**947.6**	**504.9**	**692.8**	**668.9**	**697.3**	**683.0**
Net International Reserves	215.0	169.2	577.0	505.8	517.0	839.3	524.6	849.0	465.0	628.3	611.3	638.2	631.5
Gross reserves [1, 2]	240.6	197.1	595.2	532.8	544.5	883.0	552.3	862.5	493.7	657.8	641.7	669.4	663.5
Of which: National Oil Account	0.0	0.0	276.1	102.1	104.0	474.7	106.0	498.5	110.9	190.0	196.6	203.3	210.1
Of which: guarantee deposits	25.6	17.9	6.5	14.7	15.0	30.8	15.1	0.0	0.0	0.0	0.0	0.0	0.0
Short-term liabilities [1]	-25.6	-27.9	-18.2	-27.0	-27.4	-43.7	-27.6	-13.4	-28.7	-29.5	-30.3	-31.2	-32.0
Other foreign assets	46.5	49.5	58.3	89.7	90.8	111.2	91.9	134.4	95.7	98.4	101.0	103.7	106.4
Other liabilities [3]	-26.4	-29.4	-37.4	-46.4	-46.8	-56.6	-53.6	-35.8	-55.8	-33.8	-43.4	-44.6	-54.9
Net domestic assets	**-76.4**	**-70.0**	**-387.2**	**-305.5**	**-301.9**	**-662.0**	**-289.8**	**-694.0**	**-235.4**	**-410.8**	**-366.4**	**-375.0**	**-355.5**
Net domestic credit	29.4	54.7	-234.9	-133.0	-122.8	-478.9	-108.3	-501.4	-50.9	-217.3	-163.3	-162.1	-139.7
Net credit to government	23.8	42.6	-247.9	-145.6	-135.6	-491.5	-120.5	-514.0	-63.0	-229.4	-175.4	-174.3	-151.9
Claims [3]	63.1	83.6	87.8	98.1	98.7	108.8	105.8	88.6	108.5	86.9	96.8	98.3	108.9
Of which: use of SDRs/Poverty Reduction and Growth Facility	35.0	38.9	47.8	57.6	58.1	68.3	65.1	48.1	67.7	46.2	56.1	57.6	68.2
Deposits [2]	-39.2	-41.0	-335.7	-243.7	-234.4	-600.3	-226.3	-602.6	-171.5	-316.3	-272.2	-272.6	-260.8
Ordinary	-16.0	-14.5	-15.5	-40.7	-40.6	-55.7	-49.0	-52.3	-27.2	-39.7	-27.7	-18.2	-10.0
Of which: HIPC Initiative resources	-10.3	-4.2	-3.4	-29.1	-16.7	-44.1	-20.3	-40.7	-3.5	-16.0	-14.0	-19.4	-11.3
Counterpart funds	-11.5	-16.2	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6	-22.6
Foreign currency [2]	-11.8	-10.3	-297.6	-180.3	-171.1	-522.0	-154.6	-527.7	-121.7	-254.0	-221.9	-231.8	-228.1
Of which: National Oil Account [2]	0.0	0.0	-276.1	-102.1	-104.0	-474.7	-106.0	-498.5	-110.9	-190.0	-196.6	-203.3	-210.1
Rediscount to commercial banks	1.1	5.2	5.2	3.9	3.9	3.9	2.5	3.9	2.5	2.5	2.5	2.5	2.5
Guarantee deposits from financial institutions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other claims	4.4	6.9	7.8	8.7	9.0	8.7	9.7	8.7	9.6	9.6	9.6	9.6	9.6
Certificates of deposit	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other items (net)	-105.8	-124.7	-152.3	-172.5	-179.1	-183.1	-181.5	-192.6	-184.5	-193.5	-203.2	-212.9	-215.8
Base Money	**158.7**	**119.2**	**210.6**	**243.6**	**259.2**	**232.0**	**273.2**	**253.6**	**269.5**	**282.0**	**302.5**	**322.3**	**327.6**
Currency issued	63.1	67.2	81.1	77.1	90.5	80.4	94.4	94.3	103.6	99.0	105.0	110.6	123.7
Bank reserves	95.6	52.1	129.5	166.5	168.8	151.6	178.7	159.3	165.9	182.9	197.5	211.7	203.8
Of which: domestic currency	82.4	42.0	29.9	...	58.9	...	80.5	...	83.7	...	...	...	102.8
foreign currency	13.2	10.1	99.6	...	109.9	...	98.2	...	82.2	...	...	...	101.0
Memorandum items:													
Gross International Reserves (US$ millions) [1, 2]	25.7	19.8	50.7	43.5	43.7	68.8	44.0	64.3	37.8	49.0	46.5	47.3	45.7
Of which: excluding National Oil Account and guarantee deposits	23.0	18.0	26.6	33.9	34.1	29.4	34.4	27.1	29.3	34.8	32.3	32.9	31.2
Net International Reserves (US$ millions) [2]	23.0	17.0	49.1	41.3	41.5	65.4	41.8	63.3	35.6	46.8	44.3	45.1	43.5
National Oil Account (US$ millions) [2]	0.0	0.0	23.5	8.3	8.3	37.0	8.4	37.1	8.5	14.2	14.3	14.4	14.5
Net international reserves (US$ millions; excl. National Oil Account)	23.0	17.0	25.6	32.9	33.1	28.4	33.4	26.1	27.1	32.6	30.1	30.7	29.0
Commercial banks' reserves in foreign currency	1.4	1.0	8.4	...	8.7	...	7.7	...	6.2	...	...	...	6.9
Net international reserves (US$ millions)													
(excluding NOA and banks' reserves in foreign currency)	21.6	16.0	17.3	...	24.4	...	25.6	...	20.9	...	...	...	22.1
Base money (annual percent change)	41.8	-24.9	76.6	103.7	116.8	27.1	49.6	20.4	27.9	5.0	16.7	12.1	21.5
Currency Issued (annual percent change)	38.0	6.4	20.8	50.3	76.3	38.4	62.6	16.3	27.7	-4.4	16.0	15.7	19.5

Sources: São Tomé and Príncipe authorities, and IMF staff estimates and projections.

[1] Includes guarantee deposits by prospective financial institutions waiting for operating licenses.

[2] Oil signature bonuses for Blocks 5 and 6 in JDZ, totalling US$26.1 million, originally assumed for 2006, are now projected for 2007.

[3] Includes prospective disbursements under PRGF arrangement and MDRI assistance from the IMF as a stock of debt reduction totaling SDR1.6 million assumed in the first quarter of 2007.

Table 6. São Tomé and Príncipe: Balance of Payments, 2003–10

	2003	2004	2005	2006		2007	2008	2009	2010
				CR/06/400	Proj.	Proj.			
	(Millions of U.S. dollars, unless otherwise specified)								
Current account balance (excluding official transfers) [1]	**-33.5**	**-37.8**	**-44.7**	**-68.5**	**-71.8**	**-78.2**	**-86.4**	**-94.1**	**-103.3**
Of which : non-oil current account balance [1]	-33.5	-37.8	-44.9	. . .	-57.8	-56.6	-60.4	-64.8	-70.0
Trade balance [1]	-27.0	-32.4	-38.2	-56.0	-60.0	-65.9	-71.6	-77.6	-84.7
Of which : non-oil trade balance [1]	. . .	. . .	-38.2	. . .	-49.6	-51.1	-54.8	-58.8	-63.5
Exports, f.o.b.	6.6	3.6	3.4	3.2	3.2	3.3	3.5	3.6	3.7
Of which : cocoa	6.1	3.2	3.0	3.0	3.0	2.9	2.9	3.0	3.0
Imports, f.o.b. [1]	-33.6	-36.0	-41.6	-59.2	-63.2	-69.3	-75.1	-81.2	-88.3
Food	-12.0	-12.2	-14.8	-16.4	-16.3	-18.7	-20.3	-22.4	-24.8
Investment goods [1]	-13.4	-11.6	-12.7	-16.1	-19.0	-17.9	-18.6	-19.4	-20.3
Oil sector-related investment goods [1]	0.0	0.0	0.0	-10.4	-10.4	-14.8	-16.8	-18.8	-21.2
Petroleum products	-4.7	-7.8	-9.8	-11.9	-12.8	-12.4	-13.5	-14.1	-14.8
Other	-3.5	-4.3	-4.3	-4.5	-4.7	-5.4	-5.9	-6.5	-7.2
Services and income (net)	-8.4	-7.5	-8.0	-14.0	-13.4	-13.9	-16.5	-18.3	-20.5
Exports of nonfactor services	14.1	16.6	17.7	19.3	19.3	20.5	22.0	23.6	25.3
Of which : travel and tourism	10.6	12.8	13.6	14.4	14.9	15.9	17.1	18.4	19.8
Imports of nonfactor services	-19.7	-21.0	-22.7	-30.8	-30.0	-32.6	-37.4	-40.7	-44.5
Freight and insurance	-8.4	-9.0	-10.4	-12.2	-13.2	-13.6	-14.6	-15.6	-16.8
Technical assistance	-6.0	-6.7	-6.6	-5.6	-6.9	-5.9	-6.3	-6.8	-7.2
Oil sector-related services	0.0	0.0	0.0	-4.4	-4.4	-7.2	-10.1	-11.3	-12.7
Other	-5.3	-5.4	-5.7	-8.5	-5.4	-5.9	-6.4	-7.0	-7.8
Factor services (net)	-2.8	-3.1	-3.0	-2.5	-2.7	-1.9	-1.1	-1.2	-1.4
Interest due	-2.8	-3.1	-3.2	-3.3	-3.5	-2.3	-2.1	-2.0	-2.0
Permanent oil fund interest earnings	0.0	0.0	0.2	0.8	0.8	0.4	1.0	0.8	0.7
Private transfers (net)	1.8	2.1	1.5	1.6	1.6	1.7	1.7	1.8	1.9
Official transfers (net)	20.1	23.0	22.7	22.4	25.6	22.5	24.0	25.5	27.0
Of which : public investment projects	15.2	14.9	15.5	14.2	18.7	17.7	19.2	20.7	22.2
nonproject grants	0.3	2.1	1.6	1.7	0.2	1.5	1.5	1.5	1.5
HIPC Initiative-related grants	3.2	3.2	3.2	2.5	3.4	0.0	0.0	0.0	0.0
Nigeria grant	0.1	1.4	0.9	0.8	0.8	0.8	0.8	0.8	0.8
Current account balance, including official transfers	**-13.4**	**-14.9**	**-22.1**	**-46.1**	**-46.2**	**-55.7**	**-62.4**	**-68.6**	**-76.3**
Of which : non-oil current account balance [1]	-13.4	-14.9	-22.3	. . .	-32.2	-34.1	-36.4	-39.3	-43.0
Capital and financial account balance	**2.3**	**1.9**	**53.1**	**57.4**	**30.4**	**62.2**	**79.6**	**61.9**	**71.0**
Capital transfer [2]	0.0	0.0	0.0	**2.3**	0.0	162.7	0.0	0.0	0.0
Financial account	2.3	1.9	53.1	55.1	30.4	-100.5	79.6	61.9	71.0
Public sector (net)	-0.6	2.5	29.7	19.4	-5.6	-149.9	24.7	-1.0	-1.2
Project loans	1.9	3.9	1.3	4.4	4.4	1.9	1.9	1.9	1.9
Program loans	0.0	0.0	0.0	1.0	0.0	1.5	2.0	2.0	2.0
Oil signature bonuses [3]	0.0	0.0	49.2	28.6	0.0	28.6	26.1	0.0	0.0
Amortization [4]	-7.6	-7.5	-8.9	-9.6	-5.5	-163.5	-0.9	-0.9	-0.9
Other investment	5.0	6.0	-11.9	-5.0	-4.5	-18.4	-4.4	-4.0	-4.2
Of which : Nigerian and Angola advances	5.0	6.0	0.0	0.0	2.0	0.0	0.0	0.0	0.0
repayment of Nigeria and Angola	0.0	0.0	0.0	0.0	-2.0	-15.0	0.0	0.0	0.0
transfers to JDA	0.0	0.0	-11.4	-3.7	-3.8	-3.6	-3.8	-4.0	-4.2
Private sector (net)	2.9	-0.6	23.3	35.7	36.0	49.3	54.8	62.8	72.1
Direct foreign investment	3.4	3.5	5.2	26.5	29.4	28.4	30.4	32.4	34.8
Of which : petroleum-related investment	0.0	0.0	0.0	. . .	14.8	14.8	16.8	18.8	21.2
Commercial banks	-2.0	-1.3	-8.5	6.0	4.2	0.0	0.0	-2.5	-1.0
Short-term private capital	1.5	-2.8	26.5	3.2	2.4	20.9	24.4	32.9	38.3
Errors and omissions	**13.1**	**2.0**	**1.5**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Overall balance	**1.9**	**-11.0**	**32.5**	**11.3**	**-15.8**	**6.4**	**17.2**	**-6.7**	**-5.3**

Continued

Table 6. São Tomé and Príncipe: Balance of Payments, 2003–10 (concluded)

	2003	2004	2006			2007	2008	2009	2010
			Rev. Est.	CR/06/400	Proj.	Proj.			
	(Millions of U.S. dollars, unless otherwise specified)								
Overall balance	**1.9**	**-11.0**	**32.5**	**11.3**	**-15.8**	**6.4**	**17.2**	**-6.7**	**-5.3**
Financing	-1.9	11.0	-32.5	-11.3	15.8	-6.4	-17.2	6.7	5.3
Change in net international reserves, excl. NOA (increase -)	-5.9	6.0	-8.7	-0.6	-1.6	-1.9	-2.0	-3.0	-3.5
Use of Fund resources (net) [5]	0.0	0.0	0.5	-1.0	0.7	-0.2	0.6	0.0	0.0
National Oil Account (increase -)	0.0	0.0	-23.3	-13.8	14.8	-6.0	-24.2	6.9	5.7
Change in medium- and long-term arrears (net; decrease -) [6]	4.0	5.0	-14.6	-6.5	1.9	-10.2	0.0	0.0	0.0
Debt relief (HIPC bilateral) [2]	0.0	0.0	0.2	4.6	0.0	1.7	1.6	1.6	1.6
Rescheduling arrears	0.0	0.0	13.3	5.7	0.0	10.2	0.0	0.0	0.0
Exceptional financing (Fund MDRI)	0.0	0.0	0.0	0.3	0.0	0.0	0.0	0.0	0.0
Financing gap	0.0	0.0	0.0	0.0	0.0	0.0	6.7	1.2	1.5
Memorandum items:									
Cocoa export volume (thousands of metric tons)	3.8	2.5	2.4	2.3	2.3	2.3	2.3	2.3	2.3
Cocoa export unit value (U.S. dollars per metric ton)	1,607	1,256	1,251	1,240	1,240	1,280	1,296	1,304	1,304
Scheduled external debt service before HIPC and MDRI debt relief [7]	50.3	52.3	57.2	70.2	40.1	38.3	38.5	38.2	37.3
External debt service after HIPC and MDRI debt relief [7, 8]	15.4	11.8	48.1	19.4	19.0	5.9	5.3	4.9	4.5
Current account balance, incl. official transfers (percent of GDP)	-22.7	-23.1	-30.7	-63.0	-58.6	-61.6	-63.4	-63.1	-63.4
Current account balance, excl. official transfers (percent of GDP)	-56.7	-58.8	-62.3	-93.6	-91.0	-86.5	-87.7	-86.6	-85.9
Trade balance (percent of GDP)	-45.6	-50.3	-53.3	. . .	-76.0	-72.9	-72.8	-71.4	-70.4
Gross reserves (months of following year's imports of goods and nonfactor services) [9]	4.8	3.4	4.1	4.2	4.4	4.4	4.3	4.4	4.6

Sources: São Tomé and Príncipe authorities, and IMF staff estimates and projections.

[1] From 2006, current account deficit increases reflecting higher investment-related imports of goods and services for Block 1 and foreign investment in the tourism sector.

[2] Assumes HIPC Initiative completion point and MDRI debt relief in 2007.

[3] Oil Signature Bonuses for Blocks 5 and 6 in JDZ, totaling US$26.1 million, originally assumed for 2006, are now projected for 2007.

[4] For 2007, assumes HIPC Initiative completion point and delivery of MDRI debt relief by IDA and AfDF as stock of debt reduction.

[5] For 2007, assumes MDRI assistance from the IMF as a stock of debt reduction totaling SDR 1.6 million.

[6] In 2005 includes the new Paris Club rescheduling agreement. For 2007, assumes rescheduling agreement with non-Paris Club bilateral creditors for current maturities and stock of arrears.

[7] In percent of current year exports of goods and nonfactor services; includes obligations to the IMF.

[8] Includes settlement of arrears.

[9] Gross reserves exclude the National Oil Account and guarantee deposits placed at the central bank by financial institutions pending operating licenses; imports exclude oil sector-related imports of capital goods and services.

Table 7. São Tomé and Príncipe: External Financing Requirements and Sources, 2005–08
(Millions of U.S. dollars)

	2005	2006	2007	2008
		Proj.	Proj.	
1. Gross financing requirements	**-88.9**	**-82.0**	**-274.2**	**-93.7**
Current account, excluding official transfers	-44.7	-71.8	-78.2	-86.4
Exports, f.o.b.	3.4	3.2	3.3	3.5
Imports, f.o.b.	-41.6	-63.2	-69.3	-75.1
Services and income (net)	-8.0	-13.4	-13.9	-16.5
Private transfers	1.5	1.6	1.7	1.7
Financial account	-20.9	-10.5	-184.0	-5.3
Scheduled amortization [1]	-8.9	-5.5	-163.5	-0.9
IMF repayments [2]	-0.1	-0.5	-2.1	0.0
Other public sector investment (net)	-11.9	-4.5	-18.4	-4.4
Change in external reserves (increase -)	-8.7	-1.6	-1.9	-2.0
Change in arrears (net)	-14.6	1.9	-10.2	0.0
2. Available Funding	**88.9**	**82.0**	**274.2**	**93.7**
Oil Fund (net)	25.9	14.8	22.6	1.9
Oil signature bonuses	49.2	0.0	28.6	26.1
Saving (accumulation of oil reserve fund -)	-23.3	14.8	-6.0	-24.2
Expected disbursements	24.0	30.0	188.6	27.9
Multilateral HIPC interim assistance	3.2	3.4	0.0	0.0
Capital transfers [1, 2]	0.0	0.0	162.7	0.0
Grants [3]	19.5	22.2	22.5	24.0
Concessional loans	1.3	4.4	3.4	3.9
Project loans	1.3	4.4	1.9	1.9
Program loans	0.0	0.0	1.5	2.0
Private sector (net)	24.8	36.0	49.3	54.8
IMF [4]	0.6	1.2	1.9	0.6
Financing gap	13.6	0.0	11.8	8.3
HIPC debt relief (bilateral creditors) [2]	0.2	0.0	1.7	1.6
Reschedulable arrears (bilateral creditors) [5]	13.3	0.0	10.2	0.0
Residual financing gap	0.0	0.0	0.0	6.7

Sources: São Tomé and Príncipe authorities, and IMF staff estimates and projections.

[1] For 2007, assumes delivery of enhanced HIPC Initiative completion point, and MDRI debt relief by IDA and AfDF as stock of debt reduction.

[2] For 2007, assumes MDRI assistance from the IMF as a stock of debt reduction.

[3] Includes aid in kind received from Nigeria.

[4] Includes projected disbursements under the PRGF.

[5] In 2005 includes the new Paris Club rescheduling agreement. For 2007, assumes rescheduling agreement with non-Paris Club bilateral creditors for current maturities and stock of arrears.

Table 8. São Tomé and Príncipe: Performance Criteria and Indicative Targets for 2006

(Billions of dobras, unless otherwise specified)

	2006									
	June 30				Sep. 30			Dec. 31		
	Per. criteria CR/06/349	Per. Criteria [12] with adjusters	**Memo item:** Perf. Criteria excluding oil bonuses [13]	Prel.	Ind.Target CR/06/400	Perf. Criteria [12] with adjusters	Prel.	Perf. Criteria CR/06/400	Perf. Criteria [12] with adjusters	Target [14] Rev. Prog.
1. Floor on domestic primary balance (as defined in the TMU; cumulative from beginning of year)	-72.4	-72.4	-72.4	-98.2	-110.6	-110.6	-109.6	-143.8	-143.8	-150.0
2. Ceiling on domestic primary spending (cumulative from beginning of the year) [1]	189.1	189.1	189.1	234.2	315.6	315.6	326.9	431.4	431.4	446.3
3. Ceiling on changes in net domestic financing of the government (cumulative from beginning of the year; billions of dobras at program exchange rate) [2, 3, 4]	-277.9	-474.2	78.4	98.6	-182.0	103.6	110.1	-182.7	145.3	162.3
4. Ceiling on changes in net domestic assets of the central bank (cumulative from beginning of the year; billions of dobras at program exchange rate) [2, 3, 4]	-275.9	-472.2	80.4	90.5	-180.3	105.3	107.7	-175.2	152.8	164.2
5. Floor on changes in the net international reserves of the central bank (cummulative from beginning of the year; millions of U.S. dollars) [4, 5]	29.9	48.7	-6.0	-7.6	16.3	-12.0	-7.3	14.2	-12.2	-13.5
6. Ceiling on central government's outstanding external payment arrears (stock, millions of U.S. dollars) [6]	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
7. Ceiling on the contracting or guaranteeing of new nonconcessional external debt with original maturity of more than one year by the central government or the BCSTP (stock, millions of euros) [7, 8]	1.7	1.7	1.7	1.6	1.6	1.6	1.6	1.6	1.6	1.6
8. Ceiling on the outstanding stock of external debt with original maturity of less than one year owed or guaranteed by the central government or the BCSTP (stock, millions of U.S. dollars) [9]	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Memorandum items:										
Base money (ceiling; billions of dobras)	195.0	...	...	259.2	232.0	...	273.2	253.6	...	269.5
Currency Issued (ceiling; billions of dobras)	...	...	...	90.5	80.4	...	94.4	94.3	...	103.6
Oil signature bonuses (millions of U.S. dollars, cumulative from beginning of year)	54.7	...	...	0.0	28.6	...	0.0	28.6	...	0.0
Net external debt service payments (billions of dobras at program exchange rate) [10]	-224.9	...	...	-22.3	-32.7	...	-28.5	-32.1	...	-45.8
Official external program support as defined in the TMU (billions of dobras at program exchange rate) [11]	6.1	...	...	0.0	7.2	...	6.3	27.3	...	1.9

Sources: São Tomé and Príncipe authorities, and IMF staff estimates and projections.

[1] Equal to government domestic expenditure, as defined in the TMU, excluding all interest payments.

[2] The ceiling will be adjusted downward by the cumulative negative deviation of actual from projected net payments in external debt service and the cumulative positive deviation of actual from projected disbursements of external program support and oil bonuses; it will be adjusted upward by the cumulative positive deviation of actual from projected net payments and the cumulative negative deviation of actual and projected disbursements. Higher external support will not be adjusted downward to the extent that the government uses it (up to US$1 million) for higher capital outlays.

[3] The ceiling will be adjusted downward by the amount of accumulated domestic arrears.

[4] For 2006, includes the National Oil Account at the Central Bank, consistent with CR/06/349.

[5] The floor on net international reserves will be adjusted upward (downward) by the cumulative negative (positive) deviation of actual from projected net payments in external debt service (including repayments to Nigeria), and the cumulative positive (negative) deviation of actual from projected disbursements of oil bonuses. The upward adjustment of higher than programmed external program support will not take place to the extent that the additional support is used to accommodate higher capital outlays of the government, up to US$1 million.

[6] This is a continuous performance criterion.

[7] This performance criterion applies not only to debt as defined in point No. 9 of the *Guidelines on Performance Criteria with Respect to Foreign Debt* adopted on August 24, 2000, but also to commitments contracted or guaranteed for which value has not been received

[8] With a grant element of less than 50 percent. Includes a US$2 million loan from Angola to finance a social inclusion project.

[9] Debt is defined as in point 9 of the *Guidelines (see note 7)* . Excludes three US$5 million loans disbursed by Nigeria 2002–04, to be repaid from signature bonuses in Blocks 2–4.

[10] Includes US$15 million repayment to Nigeria, originally scheduled for the first half of 2006. Program exchange rate is 10,104 dobras per U.S. dollar.

[11] In fiscal tables, valued at projected nominal exchange rates.

[12] Using adjusters for deviations in program support and net external debt service.

[13] For purposes of comparison with original program assumptions, modified to exclude delayed oil signature bonuses (not an adjuster under CR/06/349, which set conditionality for June 30, 2006).

[14] Proposed program formulated at old program exchange rates (10,104 dobras per U.S. dollar) and flows from beginning of the year (CR/06/349). See MEFP Table 1 for corresponding end-December 2006 performance criteria formulated under the new program.

Table 9. São Tomé and Príncipe: Millennium Development Goals

	1990	1994	1997	2000	2003	2004
Goal 1. Eradicate extreme poverty and hunger						
Target 1: Halve, between 1990 and 2015, the proportion of people whose income is less than one dollar a day.						
1. Population below US$1 a day (percent)	..	..	..	..	..	..
2. Poverty gap ratio at US$1 a day (percent)	..	..	..	..	..	..
3. Share of income or consumption held by poorest 20 percent (percent)	..	..	..	..	..	..
Target 2: Halve, between 1990 and 2015, the proportion of people suffering hunger.						
4. Prevalence of child malnutrition (percent of children under 5)	..	..	..	12.9	..	..
5. Population below minimum level of dietary energy consumption (percent)	..	..	..	..	..	..
Goal 2. Achieve universal primary education						
Target 3: Ensure that, by 2015, children will be able to complete a full course of primary schooling.						
6. Net primary enrollment ratio (percent of relevant age group)	..	..	85.5	97.1	..	..
7. Percentage of cohort reaching grade 5	..	..	..	61.5	..	..
8. Youth literacy rate (percent age 15–24)	..	..	..	..	..	..
Goal 3. Promote gender equality and empower women						
Target 4: Eliminate gender disparity in primary and secondary education, preferably by 2005, and to all levels of education by 2015.						
9. Ratio of girls to boys in primary and secondary education (percent)	..	..	..	92.1	..	..
10. Ratio of young literate females to males (percent ages 15–24)	..	..	..	..	..	..
11. Share of women employed in the nonagricultural sector (percent)	..	..	..	..	..	..
12. Proportion of seats held by women in the national parliament (percent)	12.0	..	7.0	9.0	9.0	9.0
Goal 4. Reduce child mortality						
Target 5: Reduce by two-thirds, between 1990 and 2015, the under-five mortality rate.						
13. Under-five mortality rate (per 1,000)	118.0	118.0	..	118.0	118.0	118.0
14. Infant mortality rate (per 1,000 live births)	75.0	75.0	..	75.0	75.0	75.0
15. Immunization against measles (percent of children under 12-months)	71.0	65.0	60.0	69.0	87.0	87.0
Goal 5. Improve maternal health						
Target 6: Reduce by three-quarters, between 1990 and 2015, the maternal mortality ratio.						
16. Maternal mortality ratio (modeled estimate, per 100,000 live births)	..	..	..	..	..	..
17. Proportion of births attended by skilled health personnel	..	..	..	58.5	..	79.8
Goal 6. Combat HIV/AIDS, malaria, and other diseases						
Target 7: Halt by 2015, and begin to reverse, the spread of HIV/AIDS.						
18. HIV prevalence among females (percent ages 15–24)	..	..	..	..	..	1.3
19. Contraceptive prevalence rate (percent of women ages 15–49)	..	..	..	29.0	..	..
20. Number of children orphaned by HIV/AIDS	..	..	..	..	..	..
Target 8: Halt by 2015, and begin to reverse, the incidence of malaria and other major diseases.						
21. Prevalence of death associated with malaria	..	..	..	..	..	..
22. Share of population in malaria risk areas using effective prevention and treatment	..	..	..	80.0	..	..
23. Incidence of tuberculosis (per 100,000 people)	136.1	126.6	120.0	113.7	107.8	107.8
24. Tuberculosis cases detected under DOTS (percent)	..	..	..	..	..	..

Continued

Table 9. São Tomé and Príncipe: Millennium Development Goals (concluded)

	1990	1994	1997	2000	2003	2004
Goal 7. Ensure environmental sustainability						
Target 9: Integrate the principles of sustainable development into policies and programs. Reverse the loss of environmental resources.						
25. Forest area (percent of total land area)	28.1	..	..	28.1	..	..
26. Nationally protected areas (percent of total land area)	..	..	..	..	..	..
27. GDP per unit of energy use (PPP $ per kg oil equivalent)	..	..	..	..	..	..
28. CO2 emissions (metric tons per capita)	0.6	0.6	0.6	0.6	..	..
29. Proportion of population using solid fuels	..	..	..	..	..	..
Target 10: Halve, by 2015, the proportion of people without access to safe drinking water.						
30. Access to improved water source (percent of population)	..	..	..	..	79.0	..
Target 11: Achieve by 2020 significant improvement for at least 100 million slum dwellers.[1]						
31. Access to improved sanitation (percent of population)	..	..	..	..	24.0	..
32. Access to secure tenure (percent of population)	..	..	..	..	..	..
Goal 8. Develop a Global Partnership for Development						
Target 16: Develop and implement strategies for productive work for youth.						
45. Unemployment rate of population ages 15–24 (total)						
Female	..	..	..	..	..	..
Male	..	..	..	..	..	..
Target 17: Provide access to affordable essential drugs						
46. Proportion of population with access to affordable essential drugs.	..	..	..	..	..	..
Target 18: Make available new technologies, especially information and communications.						
47. Fixed line and mobile telephones (per 1,000 people)	19.2	19.8	31.2	31.0	77.6	77.6
48. Personal computers (per 1,000 people)	..	..	..	..	..	..

Sources: World Development Indicators database.

[1] Targets 33–44 are excluded because they cannot be measured on a country specific basis. They are related to official development assistance, market access, and the HIPC Initiative.

Table 10. São Tomé and Príncipe: Schedule of Disbursements Under the PRGF Arrangement, 2005–08

SDR Millions	Percent of Quota	Date available	Disbursement conditions
0.423	5.7	Aug. 2005	Board approval of arrangement
0.423	5.7	Feb. 2006	Observance of PCs for end-September 2005 and completion of the first review
0.423	5.7	Aug. 2006	Observance of PCs for end-December 2005 and completion of the second review
0.423	5.7	Jan. 2007	Observance of PCs for end-June 2006 and completion of the third review
0.423	5.7	May 2007	Observance of PCs for end-December 2006 and completion of the fourth review
0.423	5.7	Nov. 2007	Observance of PCs for end-June 2007 and completion of the fifth review
0.422	5.7	May 2008	Observance of PCs for end-December 2007 and completion of the sixth review

Source: IMF.

Table 11. São Tomé and Príncipe: Indicators of Fund Credit, 2006–10

(Millions of SDRs, unless otherwise indicated)

	2006	2007	2008	2009	2010
	Projections				
Fund credit outstanding [1]					
Millions of SDRs	3.12	3.58	3.63	3.25	2.96
Millions of U.S. dollars	4.58	5.32	5.41	4.85	4.43
Percent of quota	42.16	48.38	49.05	43.92	40.00
IMF obligations					
Total charges and interest	0.03	0.03	0.02	0.02	0.02
Existing drawings	0.03	0.02	0.01	0.01	0.01
Prospective drawings	0.00	0.01	0.01	0.01	0.01
Total repayment/repurchases	0.38	0.38	0.38	0.38	0.29
Existing drawings	0.38	0.38	0.38	0.38	0.29
Prospective drawings	0.00	0.00	0.00	0.00	0.00
Fund credit as a percent of					
Export of goods and nonfactor services	20.35	22.29	21.20	17.81	15.29
Gross official reserves	15.63	17.05	16.30	13.41	11.17
Memorandum items:					
Export of goods and nonfactor services (millions of U.S. dollars)	22.51	23.86	25.52	27.26	28.99
Gross official reserves (millions of U.S. dollars)	29.30	31.19	33.19	36.19	39.69

Sources: IMF staff estimates and projections.

[1] Includes prospective disbursements under the Poverty Reduction and Growth Facility arrangement totalling SDR2.96 million (40 percent of quota).

Table 12. São Tomé and Príncipe: Financial Soundness Indicators for the Banking Sector, 2003–06
(Percent at year's end, unless otherwise indicated)

	2003	2004	2005	2006 June
Capital Adequacy				
Regulatory capital to risk-weighted assets	...	...	...	...
Percentage of banks greater or equal to 10 percent	50	25	...	...
Percentage of banks below 10 and above 6 percent minimum	...	...	...	...
Percentage of banks below 6 percent minimum	...	...	...	...
Capital (net worth) to assets	21.2	29.6	9.6	15.5
Asset quality				
Foreign exchange loans to total loans	67.4	72.1	81.2	82.4
Past-due loans to gross loans	6.0	21.6	37.6	44.4
Nonperforming loans	...	...	...	...
Watch-listed loans	...	...	...	...
Provision as percent of past-due loans	153.9	52.0	12.9	3.7
Earnings and profitability				
Net profit (before tax)/net income	...	...	...	...
Return on assets	1.1	-4.3	-11.3	-4.5
Return on equity	19.2	-10.0	-44.2	-24.1
Expense/income	...	...	...	...
Interest rate spread (deposit money banks)				
Lending rates minus demand deposit rates	...	...	...	...
Lending rates minus saving deposit rates	...	...	...	...
Liquidity				
Liquid assets/total assets	69.0	44.7	46.2	44.5
Liquid assets/short term liabilities	85.3	70.0	69.2	68.5
Loan/deposits	32.9	63.1	56.5	61.8
Foreign exchange liabilities/total liabilities	50.8	49.7	50.5	46.1
Sensitivity to market risk				
Net foreign exchange assets (liabilities) to shareholders funds	...	...	...	...

Source: Central Bank of São Tomé and Príncipe.

APPENDIX I

São Tomé, December 27, 2006

Mr. Rodrigo de Rato
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Mr. de Rato:

1. The attached Memorandum of Economic and Financial Policies (MEFP) sets out the objectives and policies that the government of São Tomé and Príncipe intends to pursue during the remainder of 2006 and for 2007, consistent with the Government's Poverty Reduction Strategy (PRS) and the objectives of the three-year arrangement under the IMF's Poverty Reduction and Growth Facility (PRGF). Based on our efforts we sincerely hope the Saotomean population will benefit from the continued support of the international community, including through debt relief. We understand that São Tomé and Príncipe would reach the completion point under the enhanced Heavily Indebted Poor Countries (HIPC) Initiative once the Board of the IMF completes the third review under the PRGF arrangement and the Boards of the IMF and World Bank determine that all completion point triggers laid out in the HIPC decision point document have been met.

2. The year 2006 has been crucial for our country as we held parliamentary, presidential and local elections which have strengthened our democratic institutions. While undertaking the elections, we have continued the progress since the beginning of our program in 2005, notably in fiscal consolidation while prioritizing social spending, in developing monetary instruments to control inflation, and in implementing structural reforms, with a focus on good governance. We have also expeditiously implemented all the HIPC completion point triggers, and we are putting in place transparent frameworks for the management of public expenditure and the use of oil resources, especially for poverty reduction. Our program through end-2007 envisages a continuation of fiscal consolidation combined with a prudent use of oil bonuses, a strengthening of monetary and exchange rate policies to lower inflation, and an acceleration of structural reforms. These are key conditions for sustained low-inflation growth which in turn is key for poverty reduction.

3. In support of our objectives and policies, the government hereby requests the completion of the third review and the disbursement of the fourth loan under the PRGF arrangement in an amount equivalent to SDR 0.423 million (5.7 percent of quota). The Government requests waivers for the nonobservance of the end-June 2006 performance criteria for domestic primary balance, domestic primary spending, and net domestic financing of the government. These deviations are mainly due to higher spending related to the elections, and the Government has since then taken revenue and expenditure measures as well as monetary policy measures to broadly safeguard the financial targets for end-2006. At end-November, these measures have allowed the domestic primary deficit in percent of GDP to return to the programmed path and 12-month inflation to slow to 24 percent from its peak

of 26 percent at end-August. The Government also requests waivers for the nonobservance of the end-June 2006 performance criteria on net international reserves and net domestic assets of the Central Bank of São Tomé and Príncipe which was mostly due to the delay in the receipt of oil signature bonuses. Given that the higher inflation and election spending needs have required a revision of our fiscal program for 2006, the Government requests modification of the targets for four quantitative performance criteria for end-December 2006; it also requests deletion of the performance criterion for domestic primary spending. Furthermore, the Government requests deletion of the structural performance criterion on the implementation of the public financial management system (SAFE) on the understanding that it will be established in due course as a structural performance criterion for end-December 2007 related to the sixth review.

4. The Government will provide the IMF with such information as the IMF may request regarding progress made in implementing the economic and financial policies and achieving the objectives of the program.

5. The fourth and fifth reviews related to the fifth and sixth disbursements under the PRGF arrangement based on the end-December 2006 and end-June 2007 performance criteria are expected for May and November 2007, respectively.

6. The Government believes that the policies and measures set forth in the MEFP are adequate to achieve the objectives of the 2006–07 program supported by the PRGF arrangement, but will take further measures to that end if deemed necessary. During the implementation of the arrangement, the Government will consult with the Managing Director of the IMF on the adoption of any measures that may be appropriate, at the initiative of the Government or whenever the Managing Director requests such a consultation.

7. The Government intends to make the contents of this Letter of Intent and those of the attached MEFP and Technical Memorandum of Understanding (TMU), as well as the staff report on the third review under the PRGF arrangement, available to the public and authorizes the IMF to arrange for them to be posted on the IMF website, subsequent to Board completion of the third review.

Yours truly,

/s/

Mrs. Maria dos Santos Tebús Torres
Deputy Prime Minister and
Minister of Planning and Finance

/s/

Mr. Alindo Afonso de Carvalho
Governor
Central Bank of São Tomé and Príncipe

Attachments: Memorandum of Economic and Financial Policies

Technical Memorandum of Understanding

APPENDIX I
ATTACHMENT I

SÃO TOMÉ AND PRÍNCIPE: MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES
December 27, 2006

I. INTRODUCTION

1. This Memorandum of Economic and Financial Policies (MEFP) supplements that of July 2006, as well as our Letter of Intent dated July 14, 2006. It describes (i) performance under the PRGF arrangement through September 2006; (ii) economic developments in the first nine months of 2006, and (iii) the government's economic program for the remainder of this year and for 2007. The satisfactory performance under the PRGF-supported program since 2005, combined with our policies set forth in this Memorandum should help São Tomé and Príncipe attain the medium-term objectives set out in our PRSP and reach the completion point for the enhanced Heavily Indebted Poor Countries (HIPC) Initiative. Our government remains committed to create the conditions for sustained low-inflationary growth, which is essential for reducing poverty.

II. RECENT ECONOMIC DEVELOPMENTS AND PERFORMANCE UNDER THE PROGRAM

2. **Economic activity so far in 2006 has exceeded expectations, with GDP growth projected at 8 percent**. The construction, commerce and services sectors have shown strong growth, while the agricultural and fishery sectors have shown lower growth due to structural problems.

3. **Inflation rose to 26 percent in the 12 months through August (from 17.2 at end-2005), as a result of a combination of temporary exogenous factors and fiscal and monetary expansion.** On the supply side, temporary food shortages and other bottlenecks and the significant increase in fuel prices to move closer to world prices in June have contributed to the surge in inflation. Large unexpected private capital inflows and related built up of foreign currency deposits (FCD), together with some unforeseen fiscal spending related to the electoral period, have boosted base money, credit to the economy, and broad money (M3).

4. **The Dobra depreciated by 10 percent against the U.S. dollar in the 12 months through November 2006**. The growth in FCD may have slowed the depreciation of the exchange rate so far in 2006.

5. **Fiscal performance deviated somewhat from the program path through June 2006 owing mainly to expenditure overruns related to the elections and the need to meet unforeseen needs, mainly in the period January–April.** Domestic primary spending was

higher than programmed reflecting (i) higher-than-programmed spending for the elections (Dobras 9 billion); (ii) unbudgeted advances by the treasury for projects pending financing by donors (Dobras 10 billion); and (iii) extrabudgetary spending for the military for back risk premia (Dobras 5 billion) committed by the previous government. Revenue collection was better than programmed thanks to more buoyant import and domestic indirect tax receipts. As a result, the performance criteria for domestic primary balance and spending were missed by the equivalent of 2 and 2½ percent of GDP, respectively. However, fiscal measures initiated in May 2006, notably the increase in import reference prices, the 28 percent increase in petroleum prices in June, and a stricter control of expenditure have started to reap benefits, bringing the domestic primary deficit close to the indicative ceiling envisaged for end-September. Our financial management was complicated by the delay in receipt of oil signature bonuses for Blocks 2–4 (a total of US$28.6 million) which led to the nonobservance of three end-June monetary performance criteria, even after adjustment for these delays.

6. **Monetary aggregates grew faster than programmed because of overperformance on net international reserves (NIR), unplanned increase in credit to government, and large increase in private foreign currency deposits (FCD) partly related to the electoral period.** The overperformance on NIR resulted from the Central Bank of São Tomé and Príncipe's (BCSTP) cautious approach to the sale of foreign exchange reserves for fear of missing NIR targets, when the receipt of oil bonuses did not materialize. Moreover, concern about an excessive depreciation of the exchange rate and its impact on inflation led to the suspension of the foreign exchange auctions and the reversion to direct sales to priority sectors, such as for oil and government needs. However, after the suspension, the BCSTP has continued to adjust its exchange rate daily to market conditions by calculating it as the sum of (i) 40 percent of the previous day's selling rate quoted by commercial banks for transactions with the public; and (ii) 60 percent of its previous day own selling rate. As a result, the emerging tensions on the foreign exchange market have remained limited and commercial bank selling rates have only relatively little deviated from that of the central bank.

7. **In response to the strong growth of monetary aggregates, the BCSTP raised its reference interest rate from 18.2 to 24 percent in May and to 28 percent in September and slightly raised reserve requirements**. However, although the program goal of keeping real interest rates positive was attained, these containment measures had only relatively little impact on the level of liquidity and monetary aggregates.

8. **Structural reforms under the program advanced considerably in 2006, compensating for the slow pace that had been registered, allowing five structural benchmarks for September to be met by December** (Table 4). The government strengthened the powers of the Inspectorate General of Finance (IGF) to oversee and audit government financial operations (presidential decree promulgated end-December); submitted two draft customs laws to the National Assembly and a related administrative text is ready for promulgation (November); and completed studies for the electricity sector (November) and for the restructuring of the port and airport (September). The government made significant progress

in preparing the integrated public financial management system for budget execution (SAFE), with the submission to the National Assembly of the organic public finance law (November), the preparation of a new budget nomenclature and a ministerial circular for a new public accounting system. However, the preparation of the SAFE and agreement on modalities with a key donor has taken longer than foreseen and its full implementation is expected for end-2007 (instead of end-2006 as planned).

9. **The government also made progress on other structural reforms to improve the business climate and enhance governance.** The remaining trigger for the HIPC Completion Point—the establishment of arbitration tribunals—was met with the promulgation of the arbitration law and the setting up of a **"center of arbitration"** at the Chamber of Commerce in mid-December. Furthermore, the government has submitted to the National Assembly the draft anti-money laundering law, ahead of schedule in October.

III. Economic Policies for the rest of 2006

10. **To reduce inflation, the authorities will vigorously implement the fiscal and monetary tightening agreed on in the second program review so as to stay close to the financial targets for end-2006, while protecting as much as possible propoor spending.** The authorities will continue to make every effort to speed up ongoing structural reforms, notably in the areas of public expenditure management and tax reform.

A. Fiscal Policy

11. **For the remainder of 2006, our government will continue to implement fiscal measures so as to contain the domestic primary deficit within the program target of 15½ percent.** The impact of the measures already implemented has allowed the domestic primary balance to be close to the indicative program targets for end-September. The revised program takes into account that the originally projected oil bonuses for blocks 2–4 (US$ 28.6 million) are unlikely to be disbursed before end-2006.

12. **On the revenue side, the government has stepped up its efforts to implement the measures agreed in May 2006** (Table 3):

- we have adopted and started implementing an action plan to recover corporate and personal income tax arrears (an estimated stock of Dobras 67 billion at end-October 2006), and the collection of ENCO indirect tax arrears on petroleum products;

- we will review the structure of the petroleum pricing mechanism as well as exemptions to eliminate existing anomalies (cross subsidies and ENCO's hidden losses) and at least safeguard petroleum revenue in percent of GDP. Based on this review and in consultation with IMF and World Bank staffs, it intends to introduce a revised structure with fewer exemptions by mid–March 2007, with a moderate increase in pump prices as needed, based on the simulations to be undertaken;

- we intend to effect the increase in excises on services (excluding water and electricity), from 5 percent to 7 percent, and raise the tax base by end-December 2006; and

- we have submitted a proposal to the National Assembly to increase excises on some imported goods, including alcoholic beverages and tobacco.

13. **On the expenditure side, we have implemented measures to correct the expenditure overruns registered in the first half of 2006**:

- the wage bill will be contained at Dobras 133 billion (equivalent to 13.5 percent of GDP, below the program figure of 13.8 percent) and wage drift due to payment of bonuses and other emoluments will be strictly monitored;

- non-wage expenditure will be vigorously contained by strict application of the May 19, 2006 budget circulars requiring prior authorization by the Minister of Planning and Finance of all expenditure commitments (*compromissos)* by budgetary units (except for spending within monthly budget allocations for wages, fuel, food, medicines, basic office supplies, and telecommunications); the payment of utilities (electricity and water) will closely follow consumption while continuing to avoid arrears; and all expenditure commitments have been stopped in early December 2006; and

- propoor spending is expected to increase to Dobras 230 billion (from Dobras 193 billion in 2005) thanks to the use of HIPC funds; however, due to the delay in the conclusion of interim debt relief agreements with bilateral creditors and the government's tight financial situation, propoor spending in 2006 will be somewhat below the program target (23.3 percent of GDP compared with 28.4 percent of GDP under the original program).

B. Monetary and Exchange Rate Policies

14. **The BCSTP's overriding objective is to reduce the rate of inflation in close coordination with fiscal policy, while maintaining a flexible exchange rate regime.** To this effect, the monetary authorities will adhere strictly to the target for base money and make a more active use of available monetary and foreign exchange instruments, consistent with the NIR target. Our monetary program envisages base money growth of 27.9 percent in 2006 and 21.5 percent in 2007. Given the high proportion of foreign currency in deposits, credit to the economy, and bank reserves (and the sensitivity of inflation to exchange rate volatility), the authorities will closely monitor the evolution of the Dobras component of base money to ensure an orderly evolution of the exchange rate. Furthermore, given the uncertainty about the relationship between base money, broad money (M3), and inflation under currency substitution, the authorities will respond flexibly to deviations from the base money target in consultation with IMF staff as needed.

15. **With a view to mopping up excess liquidity, the BCSTP will activate its instrument of Certificates of Deposits (CDs) and will introduce a complementary deposit facility**

depending on its financial position. A first issuance of CDs is envisaged for December 2006 and should help pave the way for the development of an interbank market, and in due course, open market operations. Subsequently, the BCSTP will start accepting fixed-term remunerated deposits from commercial banks in the second quarter of 2007.

16. **The BCSTP remains committed to maintaining a flexible exchange rate regime—while meeting the NIR target and avoiding excessive fluctuations of the exchange rate—through both auctions and direct sales of foreign exchange, taking into account the evolution of the foreign exchange market.** Although the daily adjustment of the BCSTP's exchange rate has avoided the emergence of significant parallel market premiums, the BCSTP aims to return before end-2006 to its single-price auctions, with a view to ensuring a fuller and faster market determination of the exchange rate, while avoiding excessive fluctuations in the exchange rate. To this effect, the BCSTP will conduct selling or buying auctions, at least bi-weekly, but it will meet banks demand for payments for petroleum imports and government needs (including scholarships and debt service) through direct sales outside the auction, at the current BCSTP exchange rate. Furthermore, the BCSTP will also strengthen its foreign exchange liquidity forecast, taking into account banks net open foreign currency positions in determining the amounts of its intervention.

17. **The BCSTP will continue to develop its communication strategy to inform the market on its monetary and exchange policies.** The BCSTP will meet at regular pre-announced intervals with the banking community and the media, to communicate the BCSTP's views on inflation and its monetary objectives. In addition, summary data on the monetary and macroeconomic aggregates will be made available to banks every month and posted on the BCSTP website.

18. **The BCSTP will further enhance the transparency of its operations and seek to improve its financial situation.** The BCSTP has posted the audited financial statements for 2005 on its website and will continue to do so every year. Its budget execution and profits and loss account on a cash basis will be reported at least quarterly as part of the program's monetary data. With regards to the construction of its new building, the BCSTP will seek to significantly reduce the total cost of the project, taking into consideration its contractual obligations and the impact on its current and future financial situation, in consultation with the government and IMF staff.

C. Structural Policies

19. **Following the submission of the main texts, the legal and institutional framework for the reform of public finance should be ready before the end of 2006.** This includes: putting in place the institutional and legal framework for the budget execution system (SAFE); the submission of six direct tax reform laws to the National Assembly; the start of implementation of the customs reform laws following their adoption by end-2006; and the

adoption by the National Assembly of the new Investment Code—which provides equal treatment for domestic and foreign investors.

IV. Economic Policies and Structural Reforms for 2007

20. **Our macroeconomic framework for 2007 aims at significantly reducing inflation by continued fiscal consolidation and tighter and proactive monetary policy.** A significant reduction in inflation should be attainable given the actions we have already taken in recent months and the non-recurrence of one-off factors that contributed to inflation in 2006, such as the private capital inflows and spending related to the electoral period. MDRI relief (after HIPC completion point) should allow significantly higher propoor spending in line with the government's PRSP objectives. In this regard, we will step up our efforts to control HIPC/MDRI spending, while progressively putting in place the integrated public financial management system (SAFE) with technical assistance from Angola, the World Bank, and other external partners.

A. Fiscal Policy

21. **The government aims to reduce further the domestic primary deficit to about 12.9 percent of GDP in 2007 (compared with 15.3 percent in 2006), while increasing propoor spending**. Fiscal consolidation under the 2007 Budget (expected to be submitted to the National Assembly by end-December 2006) would come mainly from containment of nonessential spending and the wage bill, while the revenue-to-GDP is expected to decline slightly. The domestic primary deficit would be financed by the use of part of the oil bonuses (equivalent to 8.5 percent of GDP). The main elements of the fiscal program for 2007 are:

- **Receipt of oil signature bonuses from Blocks 2–4 (**delayed from 2006), projected at US$ 28.6 million (30.6 percent of GDP). Of this amount, US$8 million will be used for the budget and the remainder—after repayment of oil-related debt to Nigeria—will be deposited in the National Oil Account (NOA) to replenish the budgetary withdrawals in 2006. The NOA should reach US$14.5 million at end-2007, for future years. If further bonuses (possibly up to US$26 million) are received for blocks 5–6 in 2007, these funds will also be deposited in the NOA, consistent with Oil Revenue Management Law (ORML).

- **Full-year impact of measures taken in 2006 and early 2007** (see ¶12 above, and Table 3). The impact of the direct tax reform would be broadly neutral in 2007, reflecting the gradual adoption of the procedural codes that would strengthen the fight against tax evasion. The entry into force of the corporate and personal income tax codes is scheduled for 2008, with a potential slight loss of revenues for that year.

- **The contribution to the Joint Development Authority (JDA)** of US$3.6 million. This contribution would depend on clarification to be obtained from the Joint Ministerial

Committee (JMC) on the disbursements of oil bonuses and the execution of the JDA budget.

- **A 20 percent increase in the wage bill to Dobras 160 billion, resulting in a decline in the wage bill-to-GDP ratio to 12.8 percent** (from 13.5 percent projected for 2006). This should leave room for further hiring in the social sectors, a slight widening of the salary range, and a general wage increase of about 18 percent to partly compensate for past inflation and the absence of a general wage increase in 2006. The authorities will closely monitor all the components of salaries and strictly limit the payments of emoluments, pending the outcome of the recently initiated study of salary structure and components. Based on this study, expected for end–April 2007, the government intends to adopt a revised salary structure with adequate incentives for public servants, as a first step of a civil service reform strategy.

- **A further increase in propoor spending** to 26.0 percent of GDP (from 23.3 percent in 2006). We aim to achieve this goal by containing nonessential primary spending by systematically applying the execution mechanisms contained in the draft Organic Budget Law. We will also strictly monitor the use of HIPC resources (about 8.5 percent of GDP in flow terms) and prospective MDRI resources (about 1 percent of GDP), while aligning allocations with PRSP priorities set out in the Priority Actions Plan for 2006–08.

22. **The proposed 2007 program is fully financed.** The fiscal plan assumes budget support from Taiwan-Province of China and the World Bank (consistent with its 2006–09 Country Assistance Strategy). To seek donor support for its Priority Actions Plan for 2006–08, the government has presented a revised list of needs in infrastructure, education, and good governance to the December 2006 Round Table in São Tomé.

B. Monetary and Exchange Rate Policies

23. **The monetary program for 2007 aims at reducing inflation through a stricter adherence to the base money target and active use of monetary and foreign exchange instruments, consistent with the NIR target (approximately 4 months of imports).** The monetary program aims to reduce the 12-month inflation to the 10–15 percent range by the end of 2007 through base money growth of 21.5 percent. Base money remains an indicative target, in light of the uncertainty about the relationships between monetary aggregates, on account of movements in bank reserves (related to new banks) and FCD. With technical assistance of the IMF's MCM, the BCSTP will seek to fine-tune its instruments so as to mop up liquidity while avoiding excessive fluctuations in the exchange rate. When liquidity conditions permit and our other monetary instruments become established, the BCSTP will seek to gradually lower the reserve requirements for banks, with due regard to other aspects of financial market development. The BCSTP will also take measures to develop the foreign exchange market, including providing information on banks' net open foreign currency positions and reducing the costs of making foreign transfers (Table 5).

C. Structural Reforms in 2007

24. **The government is committed to continue strengthening public financial management, increasing transparency of the management of prospective oil resources, and strengthening our financial system.**

25. **On public financial management (PFM), the government is implementing a pilot PFM program (SAFINHO)**, as a first step toward introducing the full system (SAFE) with the 2008 Budget. The pilot encompasses budget and treasury operations and enables the directorates of the Ministry of Planning and Finance to share a unified computerized system. We will adopt a new public accounting plan and the related manual of accounting procedures, consistent with the new organic public finance law and SAFE by end-March 2007 (structural PC, Table 2). Furthermore, we will continue our in-depth review and modernization of public finances.

26. **Transparency in the oil sector is guaranteed by the ORML.** We aim to publish the ORML handbook and submit legislation relating to the Petroleum Oversight Committee for auditing and supervision of petroleum receipts and expenditures under ORML by January 2007. Simultaneously, we intend to implement the EITI process, as expressed at the third EITI conference in Oslo in October 2006. Furthermore, we will seek to improve information sharing on the outcome of JMC meetings, on Production Sharing Contracts (PSC), and budget execution reports of the Joint Development Agency (JDA).

27. **In 2007, the government intends to conduct a study on indirect taxation.** The objective will be to review the current tax structure and expand the tax base (including by including the informal sector), with the support of international partners.

28. **Regarding the financial system, the BCSTP intends to further enhance banking supervision, strengthen its internal management in line with the IMF's safeguards assessment conducted in 2004, and implement the anti-money laundering law** (Tables 2 and 5).

- The BCSTP is strengthening its capacity to supervise licensing of new banks, devise on-site and off-site prudential indicators, and assess foreign currency positions and operating risks of banks. In this context, it will issue new prudential regulations on credit classification, liquidity, transactions with related parties, and limits on net open foreign currency positions by end-June 2007 (structural PC, Table 2). A regular system for reporting prudential ratios to IMF staff has now been established.

- Following the adoption by the National Assembly of the draft anti-money laundering law (expected for end-2006), the BCSTP intends to adopt regulations on the creation of a Central Risk Unit within the BCSTP and the "know-your-client" rules for banks in March 2007.

- Regarding the safeguards assessment, the BCSTP intends to publish the 2005 audited financial statements and adopt investment guidelines for international reserves by January 2007.

29. **The government remains committed to accept the obligations under Article VIII, Sections 2(a), 3, and 4 of the IMF's Articles of Agreement, in the near future, as foreign exchange market conditions normalize.** To this effect, the exchange restriction on transfers abroad of dividends will be eliminated with the new Investment Code (expected to be adopted by the National Assembly in December 2006). Furthermore, the BCSTP expects to progressively reduce the exchange restriction related to the mechanism for selling foreign exchange to banks with the implementation of a single-price auction system and the continued application of the formula for calculating the BCSTP rate.

D. HIPC Completion Point and MDRI

30. **Reaching the HIPC completion point in early 2007 is an overriding policy objective for our government.** We believe we have made significant progress in (i) implementing the required health and education measures; (ii) putting in place institutional mechanisms to ensure efficient and transparent use of HIPC interim debt relief; and (iii) increasing transparency and accountability in the management of public resources. The remaining outstanding trigger for the HIPC completion point—the establishment of arbitration tribunals—was promulgated and is expected to be operational by end-December 2006. Furthermore, in preparation for the HIPC completion point, the government has contacted the Paris Club creditors with a view to concluding bilateral agreements under the September 2005 Paris Club terms of reference. It has also signed agreements with Germany and France, and the signature process with Spain is advanced.

31. **The government intends to use potential MDRI resources in line with the Priority Actions Program (PAP) for 2006-08.** Savings on debt service from MDRI are estimated at about 1 percent of GDP in 2007 and 2 percent on average during 2008–10. On debt management, the government is conscious of the need to secure concessional external financing and ensure debt sustainability after HIPC and MDRI. To improve the government's capacity to manage external debt, we are putting in place a debt recording and management system obtained from the Commonwealth Secretariat (CS-DRMS).

E. External Sector Policies

32. **In the context of the Integrated Framework, the government continues implementing the 2005 Diagnostic Trade Integration Study (DTIS).** Our policy aims to facilitate and expand export-oriented production by the poor, improve the business environment, enhance infrastructure and public services, and reduce trading costs. The government has appointed a commission to prepare the Memorandum on Foreign Trade Regime to be submitted

to the WTO working party as part of the formal WTO's accession. Also, the Ministry of Trade will hire a consultant to study São Tomé and Príncipe's options for regional trade integration.

F. PRSP Issues

33. **As indicated in our first PRSP Annual Progress Report, the government will continue its reforms and seek to enhance propoor spending.** Based on current trends, many MDGs may be out of reach for 2015; therefore, we have stepped up our efforts to mobilize donor support, seek enhanced donor coordination, and improve the quality of poverty reduction spending. As noted above, we have hosted sectoral Round Tables in December 2006 on governance, education, and infrastructure. We will also reinforce the PRSP monitoring and evaluation process, strengthen the Poverty Observatory (with UNDP and AfDB assistance), and seek to involve more our civil society in the implementation of the PRSP and the oversight of the use of HIPC funds.

G. Statistical Issues and Capacity Building

34. **Despite progress in certain areas (especially in monetary statistics), the government is aware of remaining weaknesses in statistical data, in particular, in the area of government financial operations (TOFE), for which the government will seek further technical assistance from the IMF.** Furthermore, the government will request technical assistance from the IMF in the areas of tax reform (notably customs and indirect taxes) and public financial management.

H. Program Monitoring

35. **The revised Technical Memorandum of Understanding (TMU) sets out the modalities of program monitoring.** This includes the definitions of performance criteria and indicative targets, the application of adjustors for deviations from programmed amounts of oil signature bonuses, budget support, and net external debt service payments, and data sources and frequency of data reporting. To strengthen program monitoring and data reporting, the government will establish an interministerial technical committee.

36. **The attached Table 1 shows the proposed quantitative performance criteria for end-December 2006 (fourth review under the program) and proposed quantitative performance criteria for end-June 2007 (fifth review).** The government requests the modification of the targets for four quantitative performance criteria (domestic primary balance, net bank financing of the government, and net domestic assets and net international reserves of the BCSTP) and the deletion of one quantitative performance criterion (domestic primary spending, already covered under the domestic primary balance) for end-December 2006, for the fourth review.

37. **The attached Table 2 includes the proposed structural performance criteria and benchmarks for December 2006 and for 2007.** The Government requests the deletion of one structural performance criterion (implementation of SAFE) for end-December 2006, on the

understanding that it will be established as a structural performance criterion for end-December 2007, for the sixth review. In addition, the non accumulation of external payment arrears (as defined in the attached revised TMU) is a continuous performance criterion, as are the injunctions against imposing or intensifying restrictions on current payments, introducing or modifying multiple currency practices, concluding bilateral payments agreements that are inconsistent with Article VIII, or imposing or intensifying import restrictions for balance of payments reasons.

Table 1. São Tomé and Príncipe: Performance Criteria and Indicative Targets for 2006–07

(Billions of dobras, unless otherwise specified)

	2006			2007			
	Sep. 30	Dec. 31		Mar. 31	Jun 30	Sep. 30	Dec. 31
	Base (in stocks)	*Perf. Criteria* [11] *CR/06/400*	Proposed revised Perf. Criteria	Ind.Target	Perf. Criteria	Ind.Target	Ind.Target
1. Floor on domestic primary balance (as defined in the TMU; cumulative from beginning of year)	...	*-143,8*	-150,0	-40,6	-97,0	-129,3	-163,2
2. Ceiling on changes in net bank financing of the government (cumulative from end–September 2006; billions of dobras at program exchange rate) [1,2, 3]	-126,8	*-182,7*	62,1	-90,3	-32,4	-23,9	3,0
3. Ceiling on changes in net domestic assets of the central bank (cumulative from end–September 2006; billions of dobras at program exchange rate) [1,2,3]	-289,8	*-175,2*	73,1	-77,7	-19,6	-11,0	21,8
4. Floor on changes in the net international reserves of the central bank (cumulative from end–September 2006; millions of U.S. dollars) [3,4]	41,8	*14,2*	-6,4	4,6	1,9	2,5	0,7
5. Ceiling on central government's outstanding external payment arrears (stock, millions of U.S. dollars) [5]	...	*0,0*	0,0	0,0	0,0	0,0	0,0
6. Ceiling on the contracting or guaranteeing of new nonconcessional external debt with original maturity of more than one year by the central government or the BCSTP (cumulative flows from January 2005, millions of euros) [6, 7]	...	*1,6*	1,6	1,6	1,6	1,6	1,6
7. Ceiling on the outstanding stock of external debt with original maturity of less than one year owed or guaranteed by the central government or the BCSTP (stock, millions of U.S. dollars) [8]	...	*1,0*	1,0	1,0	1,0	1,0	1,0
Memorandum items:							
Base money (ceiling; billions of dobras)	273,2	*...*	269,5	282,0	302,5	322,3	327,6
Currency Issued (ceiling; billions of dobras)	94,4	*94,3*	103,6	99,0	105,0	110,6	123,7
Oil signature bonuses including accrued interest on NOA (millions of U.S. dollars, cumulative from beginning of year)	0,5	*28,6*	0,6	28,7	28,8	28,9	29,0
Net external debt service payments (cumulative from beginning of the year, billions of dobras at program exchange rate) [9]	-35,4	*-32,1*	-46,1	-205,8	-211,0	-216,6	-220,4
Official external program support (cumulative from beginning of the year, billions of dobras at program exchange rate) [10]	7,8	*27,3*	2,4	0,0	0,0	31,4	41,8

Sources: São Tomé and Príncipe authorities, and IMF staff estimates and projections.

[1] The ceiling will be adjusted downward (upward) by the cumulative negative (positive) deviations of actual from projected net payments in external debt service and the cumulative positive (negative) deviation of actual from projected disbursements of external program support and oil bonuses including accrued interest on NOA. The downward adjustment of higher than programmed external program support will not take place to the extent that the additional support is used to accommodate higher capital outlays of the government, up to US$1 million.

[2] The ceiling will be adjusted downward by the amount of accumulated domestic arrears.

[3] Includes the National Oil Account (NOA) at the Central Bank.

[4] The floor on net international reserves will be adjusted upward (downward) by the cumulative negative (positive) deviation of actual from projected net payments in external debt service (including repayments to Nigeria), and the cumulative positive (negative) deviation of actual from projected disbursements of oil bonuses including accrued interest on NOA. The upward adjustment of higher than programmed external program support will not take place to the extent that the additional support is used to accommodate higher capital outlays of the government, up to US$1 million.

[5] This is a continuous performance criterion.

[6] This performance criterion applies not only to debt as defined in point No. 9 of the *Guidelines on Performance Criteria with Respect to Foreign Debt* adopted on August 24, 2000, but also to commitments contracted or guaranteed for which value has not been received.

[7] With a grant element of less than 50 percent. Includes a US$2 million loan received from Angola to finance a social inclusion project.

[8] Debt is defined as in point 9 of the *Guidelines on Performance Criteria with Respect to Foreign Debt* adopted on August 24, 2000. Excludes US$15 million in loans from Nigeria during 2002–04, which are to be repaid from signature bonuses in 2007.

[9] Includes US$15 million repayment to Nigeria.

[10] Official external program support, as defined in TMU, valued at program exchange rate of 12,549 dobras per U.S. dollar (valued at projected average exchange rate of 13,935 dobras per U.S. dollar in fiscal table).

[11] Net domestic assets of the BCSTP and net bank financing of the government measured at previous program exchange rate of 10,104 dobras per US dollar and in flows with respect to end–December 2005. In addition it assumed inflow of signature bonuses totaling US$28.6 million (reflected also in net international reserves target of BCSTP).

Table 2. São Tomé and Príncipe: Structural Performance Criteria and Benchmarks Under PRGF Arrangement, December 2006–December 2007

Action	Date
Prior Actions	
Submission to the National Assembly of the draft 2007 Budget agreed with IMF staff.	December 31, 2006
Adoption by the government of a budget nomenclature with functional, economic, and administrative classifications, based on the 2001 GFS, identifying propoor expenditure.	December 31, 2006
Issue a central bank regulation on banks' reporting of their net open foreign currency positions.	December 2006
Structural Benchmarks or Structural Performance Criteria (SPC)	
Public Expenditure Management	
Adopt decree establishing the new public accounting plan and the related manual of accounting procedures, consistent with the organic public finance law and the public financial management system (SAFE).	March 31, 2007, **SPC**
Implement the fully integrated computerized public financial management system (SAFE) with new nomenclature, unified current and investment budgets, and incorporating public accounting (including of patrimony/debt).	December 2007
Public Enterprises	
Finalize the installation of prepaid electricity metering systems (3,000).	June 2007
Oil Transparency	
Publish the Handbook of the Oil Resource Management Law (ORML) by posting it on the government website.	January 2007
Adopt Petroleum Sector Strategy for development of the Exclusive Exploitation Zone (EEZ).	December 2007
Banking Supervision	
Issue regulations to implement the law against money laundering and the financing of terrorism (AML/CFT), notably for the Central Risk Unit within the BCSTP and "know-your-client" rules for banks.	March 2007
Issue new prudential regulations on credit classification, liquidity, transactions with related parties, and limits on net open foreign currency positions.	June 30, 2007, **SPC**

Table 3. São Tomé and Príncipe: Tax Policy and Business Climate Measures November 2006–December 2007

Actions	**Dates**
Adopt and start implementing action plan to collect income tax arrears (Dobras 67 billion at end-October 2006), following adoption of new tax procedural law.	March 2007
Increase excise tax on services (excluding water and electricity) from 5 to 7 percent and enlarge tax base to include all sales except a list of exempted goods.	December 15, 2006
Domestic petroleum product pricing and tax collection:	
• Revise petroleum pricing structure, fixing distribution margins in U.S. dollar cents per liter (including for ENCO), reducing tax differentials between products, and partially moving to specific taxation, while at least safeguarding petroleum tax revenue in percent of GDP.	March 2007
• Apply revised petroleum pricing mechanism.	Continuous
• Eliminate import and consumption tax exemptions, except for EMAE and justified conventions, and eliminate Road Fund tax exemption for EMAE.	March 2007
• Adopt timetable to gradually phase out tax exemptions for EMAE.	June 2007
Submit draft direct tax reform laws to National Assembly:	December 2006
• New tax administrative and procedural codes and new inheritance tax code (for implementation in 2007).	
• New corporate tax code (for implementation in 2008).	
• New personal income tax code and new urban property tax code (for implementation in 2008).	
• Implement Investment Code (after adoption by National Assembly, expected for end-2006).	June 2007
• Draft revised Labor Code in consultation with IMF and World Bank staffs.	December 2007
• Promulgate legislation on arbitration tribunals in business and contract matters.	November 2006
• Adopt convention between Ministry of Justice and Chamber of Commerce to operationalize arbitration tribunals within Chamber of Commerce.	December 2006

Table 4. São Tomé and Príncipe: Structural Performance Criterion and Benchmarks Under the PRGF-Supported Program (March–December 2006)

Policy Measure	Test Date	Status
Structural Benchmarks		
Establish a database to record and monitor follow-up actions on problems identified by the Inspectorate General of Finance (IGF) in each inspected sector within its jurisprudence, including the applicable sanctions and penalties.	End of June 2006	Met.
Amend the laws defining internal control and administrative regulations governing the Inspectorate General of Finance (IGF) to increase IGF powers regarding the oversight and auditing of the financial operations of the central government, public enterprises, and local governments.	End of July 2006	Met in December 2006.
Submit to the National Assembly proposals to revise the Customs Law, the Customs' Organic Law (*Estatuto das Alfandegas*), and the General Code on Customs Infractions (*Regime Geral das Infrações Aduaneiras*); to update accounting practices and customs procedures; and to modernize the system to increase the efficiency of the customs service.	End of September 2006	Met in November 2006.
Complete the installation of EMAE's pre-paid electricity metering systems in designated urban locations to address the public utilities' financial weaknesses in the short run.	End of September 2006	Ongoing; installation of 3,000 meters is expected to be completed in second quarter of 2007.
Adopt a sectoral strategy to address the development of suitable infrastructure for electricity production, transportation, and distribution, as well as business modalities to secure dynamic private sector participation in the electricity sector.	End of September 2006	Met in November 2006.
Complete feasibility studies on the restructuring of ENASA and ENAPORT.	End of September 2006	Met.
Implement the Commonwealth Secretariat debt recording management system (CS-DRMS) to improve the government's capacity to manage external debt.	End of December 2006	Ongoing.
Submit to the National Assembly legislation criminalizing money laundering and the financing of terrorism.	End of December 2006	Met in October 2006.
Structural Performance Criterion		
Implement the fully integrated, computerized budget and public expenditure system ("SIGFE", renamed "SAFE").	End of December 2006	Ongoing. It is proposed to re-schedule the measure to end-December 2007.

Table 5. São Tomé and Príncipe: Monetary Policy and Banking Supervision Measures

Recommendation	Status	Date
Licensing		
• Establish contacts with Nigeria's and CEMAC's banking supervisors to cooperate and share information	Ongoing	NA
• Check background of proposed shareholders and administrators	Ongoing	NA
• Monitor implementation of business plan and performance of new bank in relation to plan	Ongoing	NA
• Increasing the minimum capital required initially	Pending	March 2007
• Qualification of administrators	Draft NAP elaborated	December 2006
Prudential Regulations		
• Revised capital adequacy minima	NAP considered	March 2007
• Liquidity	Update pending	March 2007
• Transactions with related parties	Update pending	March 2007
• Classification of Assets	Update pending	March 2007
• Credit to Employees	Update pending	March 2007
• Intervention in banks	Pending	March 2007
• Limits on banks' net open foreign currency positions	Drafted and pending	March 2007
Internal Control and Auditing		
• Implementing internal control and auditing	In progress	January 2007
• Chart of Accounts	Submitted to banks for comments	Adoption in January 2007
• Report on Financial Conditions	Pending	Adoption in January 2007
Banking Supervision		
• Timely reporting	Ongoing	NA
• Manual for on-site inspections	Manual completed and training	December 2006
• Further training with expert guidance on monitoring	Ongoing	November 2006
Monetary Policy Instruments		
• Restart the auctions of foreign exchange	Pending	December 2006
• Introduce BCSTP CDs	Pending	December 2006
• Require remunerated reserves	Pending	March 2007
• Institute a complementary deposit facility	Pending	March 2007
• Improve liquidity forecast and coordination with Treasury	Pending	June 2007
Measures for the Exchange Market		
• Implement mandatory weekly reporting to BCSTP on their net open foreign currency positions by banks	Draft of NAP	December 2006
• Implement a registry system for banks' exchange operations (including exports and imports) in order to modernize the information on trade balance and	Pending	March 2007

Recommendation	Status	Date
payments, as well as customs control (such a system is being developed at the BCSTP) • Review NAP 13/2006 to remove commission charges by BCSTP on withdrawal of foreign currency deposited by banks in the Central Bank	Done	December 2006
Communication Strategy for Monetary and Exchange Policy		
• Central bank will announce its policy objectives and framework to the public • Central bank board decisions will be explained through press notes • Regular meetings with market participants • Post BCSTP data on inflation and monetary base on website	Ongoing Ongoing Ongoing Done	NA NA NA November 2006
Anti-Money Laundering		
• Regulations for application of the law • Regulations on Credit Risk Unit and "Know your client"	Pending (draft elaborated, approval depends on passing legislation on money-laundering) Pending	March 2007 March 2007
Safeguards Assessment		
• Establish formal procedures to ensure that monetary data used to check the conformity with performance criteria within a future PRGF program follow the Technical Memorandum of Understanding of that program and are compatible with the accounting registry. The Internal Audit Department must review and certify these data. • Review the role of the Audit Board to fully align its responsibilities with those of an independent audit committee • Develop annual audit plans based on a risk analysis of operations • Introduce formal investment guidelines identifying the allowed investments, qualified counterparts, and controls of investment operations	In progress Pending Pending Pending	June 2007 June 2007 June 2007 January 2007

APPENDIX I

ATTACHMENT II

SÃO TOMÉ AND PRÍNCIPE: TECHNICAL MEMORANDUM OF UNDERSTANDING

December 27, 2006

1. This technical memorandum of understanding (TMU) contains definitions and adjuster mechanisms that are intended to clarify the measurement of variables in Table 1, Quantitative Performance Criteria, PRGF Arrangement, 2006–07, attached to the Memorandum of Economic and Financial Policies. Unless otherwise specified, all quantitative performance criteria and benchmarks will be evaluated in terms of cumulative flows from end-September, 2006.

Provision of data to the Fund

2. Data with respect to all variables subject to performance criteria and indicative targets will be provided to IMF staff on a monthly basis with a lag of no more than three weeks for data on the net domestic assets and net international reserves of the Central Bank of São Tomé and Príncipe (BCSTP), and six weeks for other data. The authorities will transmit promptly to IMF staff any data revisions. For variables that are relevant for assessing performance against program objectives but are not specifically defined in this memorandum, the authorities will consult with IMF staff as needed on the appropriate way of measuring and reporting. Performance criteria included in the program, as defined below, refer to domestic primary balance of the central government, net bank financing of the central government, net domestic assets and net international reserves of the central bank, external payments arrears, nonconcessional medium and long-term external debt and short-term external debt.

Definitions

3. **Government** is defined for the purposes of this TMU to comprise the central government, which includes all governmental departments, offices, establishments, and other bodies which are agencies or instruments of the central authority of São Tomé and Príncipe. The central government does not include the operations of state-owned enterprises.

4. **Government domestic (non-oil) revenue** comprises all tax and non-tax revenue of the government (in domestic and foreign currency), excluding foreign grants, the receipts from the local sale of in-kind grants (e.g., crude oil received from Nigeria, food aid, etc.), and any gross inflows to government on account of oil signature bonus receipts and accrued interest in the National Oil Account (NOA). Revenue will be measured on a cash basis as reported in the table of government financial operations prepared by the Directorate of Budget and Directorate of Treasury in the Ministry of Planning and Finance.

5. **Domestic primary expenditure** comprises all government spending assessed on a commitment basis (*compromisso*), excluding: (i) foreign-financed capital expenditure; (ii) foreign-financed expenditure under the overseas scholarship program that is externally-financed; and (iii) scheduled interest payments. Reporting of government domestic expenditure will be based on the government budget execution prepared every month by the Directorate of Budget and Directorate of Treasury in the Ministry of Planning and Finance.

6. Within the above total, **propoor expenditure** refers to government outlays recorded in the budget nomenclature that have a direct effect in reducing poverty, as agreed with the IMF and World Bank staffs. These expenditures, which include both current and capital outlays, are defined as follows:

a. **Propoor current spending**: These cover the following ministries and expenditure categories (by budget code) as described in the matrix below.

Code	Description of current expenditure	EDUCATION OF EDUCATION AND CULTURE	MINISTRY OF HEALTH	MINISTRY OF LABOR AND SOLIDARITY
01.00.00	Despesa com Pessoal	X	X	
02.01.05	Outros bens duradouros	X	X	
02.02.02	Combustíveis e lubrificantes	X	X	
02.02.04	Alimentação		X	
02.02.05	Medicamentos	X	X	
02.02.06	Roupas e calsados		X	
02.02.09	Outros bens não duradouros		X	
02.03.01.0	Agua e energia	X	X	
02.03.02	Conservação de bens		X	
02.03.06	Comunicações	X	X	
04.01.01	Orçamento do estado		X	
04.02.01	Instituições particulares		X	X
04.03.01	Particulares		X	X
04.04.02	Outras transferências para exterior			X
06.01.00	Ensino e formação	X		
06.04.01	Custos recorrentes de projectos	X	X	
06.04.04.0	Outros Diversos	X	X	

Expenditures on fuels and lubricants *(combustíveis e lubrificantes)* that are effected for administrative purposes are excluded. Likewise, food *(alimentacão)* and clothing and shoes *(roupas e calsados)* supplied to administrative staff are excluded.

For 2007 onwards, the definition of propoor current spending will be based on the new budget classification.

b. **Propoor capital spending:** This covers selected projects, which are deemed to have a direct impact on alleviating poverty in the following sectors: education, health, social safety nets, agriculture and fisheries, rural development, planning and finance, youth and sports, provision of potable water, and electrification.

7. **The domestic primary balance** is defined as the difference between government domestic (non-oil) revenue and domestic primary expenditure. This balance for end-September 2006 was assessed at dobras -109.6 billion, broken down as follows:

Government domestic (non-oil) revenue:	Db 217.3 billion
Less: government primary expenditure (as defined in paragraph 5)	Db 326.9 billion
Equals: domestic primary balance:	Db -109.6 billion

8. **Domestic arrears** are defined as the difference between expenditure on a commitment basis and cash payments.

9. **The program exchange rate** for the purposes of this TMU will be Db 12,548.5 per U.S. dollar. The exchange rate of the dobra against the Euro will be 15,952.93 and against the SDR will be 18,526.31.

10. **Net bank financing of the central government (NCG)** is defined as the stock of all outstanding claims on the government held by the BCSTP, less all deposits held by the central government with the BCSTP, plus the stock of all outstanding claims on the government held by deposit money banks (DMBs)[1], less all deposits held by the central government with DMBs—as they are reported monthly by the BCSTP to the IMF staff. All foreign exchange denominated accounts will be converted to dobras at the program exchange rate. At end-September 2006, outstanding net bank financing of the government was assessed at dobras -126.8 billion, broken down as follows:

BCSTP credit, including use of IMF resources:		Db 105.8 billion
Less: government deposits with BCSTP:		Db 226.3 billion
Of which:	National Oil Account (NOA)	Db 106.0 billion
	Treasury foreign currency denominated accounts	Db 43.9 billion
	Treasury local currency denominated accounts	Db 28.7 billion
	Account for HIPC relief [2]	Db 20.3 billion

[1] Deposit money banks (DMBs) refers to Other Depository Corporations as stated in the Monetary and Financial Statistics Manual.

[2] Pending the use of HIPC debt relief for pro-poor spending.

Account for MDRI relief [3]	Db 0.0 billion
Counterpart deposits	Db 22.6 billion
PRGF disbursement account	Db 4.7 billion
Equals: Net credit to government by the BCSTP:	Db -120.5 billion
Plus: DMBs credit:	Db 0.0 billion
Less: government deposits with DMBs (including counterpart funds):	Db 6.3 billion
Equals: Net bank financing of the government:	Db -126.8 billion

11. **Base money** is defined as the sum of currency issued—which consists of currency outside banks and cash in vaults—and bank reserves, at the program exchange rate. Bank reserves refer to reserves of commercial banks held with the central bank, and include reserves in excess of the legal reserve requirements. At end-September 2006, base money was assessed at dobras 273.2 billion, calculated as follows:

Currency issued:		Db 94.4 billion
Of which:	Cash in vaults:	Db 13.7 billion
	Currency outside banks:	Db 80.7 billion
Plus: Bank reserves:		Db 178.7 billion
Of which:	in dobras	Db 80.5 billion
	in foreign currency	Db 98.2 billion
Equals: Base money:		Db 273.2 billion
Of which:	in dobras	Db 175.0 billion

12. **Net international reserves** (NIR) of the BCSTP are defined for program monitoring purposes as short-term foreign assets of the BCSTP minus short-term external liabilities. All short-term foreign assets that are not fully convertible external assets readily available to and controlled by the BCSTP (i.e., they are pledged or otherwise encumbered external assets, including, but not limited to, the HIPC umbrella SDR account, and assets used as collateral or guarantees for third party liabilities) will be excluded from the definition of NIR. All values are to be converted to U.S. dollars at actual market exchange rates prevailing at the test date. At end-September 2006, NIR was assessed at dobras 524.6 billion, calculated as follows:

Net international reserves:		Db 524.6 billion
Of which:	gross reserves:	Db 552.3 billion
	Of which: National Oil Account (NOA)	Db 106.0 billion
	short-term liabilities:	Db -27.6 billion

[3] Pending the use of MDRI relief for pro-poor spending.

Plus: Other foreign assets:	Db 91.9 billion
Plus: Medium and long- term liabilities:	Db -53.6 billion
Equals: Net Foreign Assets:	Db 563.0 billion
Memorandum item:	
Net international reserves minus National Oil Account (NOA) minus bank's foreign currency deposits with the central bank	Db 320.4 billion

13. **Net domestic assets** of the central bank of São Tomé and Príncipe are defined as the difference between base money and net foreign assets of the BCSTP, all at programmed exchange rates. All foreign denominated accounts will be converted to dobras at the program exchange rate. At end-September 2006, net domestic assets were assessed at dobras–289.8 billion, calculated as follows:

Base money:	Db 273.2 billion
Less: Net foreign assets:	Db 563.0 billion
Equals: Net domestic assets of the BCSTP:	Db -289.8 billion

14. **Treasury deficit** of the Central Bank of São Tomé and Príncipe is defined as revenue (excluding unrealized valuation changes) minus costs minus investment.

15. The performance criterion on **short-term external debt** refers to the outstanding stock of external debt with original maturity of one year or less, (including overdraft positions) and owed or guaranteed by the government or the BCSTP.[4] At end-September 2006, the stock of short-term external debt stood at US$16.0 million.[5]

16. The performance criterion on **nonconcessional medium- and long-term external debt** refers to the contracting or guaranteeing of external debt with original maturity of more than one year by the government or the BCSTP.[6] [7] Debt rescheduling and restructurings are

[4] The term "debt" is defined in accordance with point 9 of the *Guidelines on Performance Criteria with respect to Foreign Debt* (Decision No. 12274-(00/85) August 24, 2000).

[5] This amount includes three nonconcessional loans from Nigeria totaling US$15 million, which were previously classified under nonconcessional medium term external debt. These loans have been reclassified as short-term debt, following a joint World Bank-IMF DSA mission in April 2006.

[6] This performance criterion applies not only to debt as defined in point No. 9 of the *Guidelines on Performance Criteria with Respect to Foreign Debt* adopted on August 24, 2000 but also to commitments contracted or guaranteed for which value has not been received.

[7] The concessionality of loans is assessed according to the reference interest rate by currency published by the Development Assistance Committee of the Organization for Economic Cooperation and Development (OECD). For loans of terms of no less than 15 years, the ten-year average of commercial interest reference rates (CIRR) for the currency in which the loan is denominated will be used. For loans of shorter terms, the six-month average will apply. A loan is deemed to be on concessional terms if, on the initial date of disbursement, the ratio of the present value of the loan, calculated on the basis of the reference interest rate, to the nominal value of the

(continued)

excluded from the ceilings set on nonconcessional borrowing. Medium- and Long-term debt will be reported by the Debt Management Unit of the Ministry of Finance and Planning and (as appropriate) by the BCSTP, measured in U.S. dollars at current exchange rates. The government of São Tomé and Príncipe will consult with IMF staff before contracting obligations if it is uncertain as to whether those obligations are included in the performance criterion limits.

17. The nonaccumulation of new **external payment arrears** is a continuous performance criterion. Government external payment arrears are defined as all unpaid external public debt obligations, according to the data established by the Debt Management Unit of the Ministry of Planning and Finance and (as appropriate) by the BCSTP, with the exception of arrears pending rescheduling arrangements. The latter will be considered technical arrears. Debt would be deemed to be in arrears when it has not been paid by the time it is due, unless the definition of an arrear has been otherwise contractually defined. The performance criterion relating to external arrears does not apply to external arrears pending the signing of bilateral agreements in the context of debt rescheduling with the Paris Club and other bilateral creditors.

18. **Net external debt service payments** are defined as debt service due less interim HIPC debt relief (including multilateral and bilateral relief) and the accumulation of any new external payment arrears, including technical arrears.

19. **Official external program support** is defined as grants and loans including in-kind aid when the products are sold by the government and receipts are freely usable by the budget, and other exceptional financing provided by foreign official entities and received by the budget. Amounts assumed in the program consistent with this definition are shown in the memorandum item entitled "official external program support" of Table 1.

Use of adjusters

20. **Deviations in receipts of oil signature bonuses including accrued interest on NOA, in official external program support, and in net external debt service payments,** from the amounts projected under the program (see Table 1) will trigger adjustments for net bank financing of the central government, net domestic assets of the BCSTP and net international reserves as indicated below. These deviations will be calculated cumulatively from end-September, 2006.

21. **Ceilings on net bank financing (NCG) of the central government and net domestic assets (NDA) of the BCSTP.** Monthly differences between actual and projected

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loan is less than 50 percent (in other words, a grant element of at least 50 percent). For currencies with no available reference interest rates, the SDR rate will be used. This performance criterion does not apply to IMF resources.

receipts of oil signature bonuses including accrued interest on NOA, official external program support, and net external debt service payments in foreign exchange will be converted to dobras at the program exchange rate, and aggregated from end-September 2006 to the test date. The ceilings on NCG and NDA will be adjusted downward (upward) by the positive (negative) sum of the deviations of actual from projected receipts of oil signature bonuses including accrued interest on NOA, actual from projected official external program support, and projected from actual net external debt service payments. In the case of a negative sum of deviations (i.e., an overall shortfall), these ceilings will be increased by 100 percent of any cumulative shortfall. In case of a positive sum (i.e., an overall surplus), the downward adjustment to NCG and NDA will not take place to the extent that additional external program support is used to accommodate higher capital outlays by the government, up to US$1 million, converted to dobras at program exchange rates.

22. **Floor on net international reserves (NIR) of the BCSTP.** The quarterly difference between actual and projected receipts of oil signature bonuses including accrued interest on NOA, official external program support, and net external debt service payments will be converted to dobras at the program exchange rate, and aggregated from end-September 2006 to the test date. The floor on NIR will be adjusted upward (downward) by the positive (negative) sum of the deviations of actual from projected receipts of oil signature bonuses including accrued interest on NOA, actual from projected official external program support, and projected from actual net external debt service payments. In the case of a negative sum of deviations (i.e., an overall shortfall), this floor will be decreased by 100 percent of any cumulative shortfall. In case of a positive sum (i.e., an overall surplus) the upward adjustment to NIR will not take place to the extent that additional external program support is used to accommodate higher capital outlays by the government, up to US$1 million, converted at program exchange rates. In addition, the NIR floor will be lowered by the amount that disbursements under the PRGF arrangement are lower than expected.

Data reporting

23. The following information will be provided to the IMF staff for the purpose of monitoring the program.

i. Fiscal data

The Directorate of Budget at the Ministry of Planning and Finance will provide to IMF staff, within two months after the end of each month or quarter, with the exception of the public investment program (PIP), which will be provided three months after each quarter:

- Monthly data on central government operations for revenues, expenditure and financing including detailed description of net earmarked resources (*recursos consignados*)
- Monthly data on net credit to the government by the BCSTP, recorded account by account in a format fully compatible with the monetary accounts of the BCSTP

- Monthly data detailed tax and non-tax revenues
- Monthly detailed data on current and domestically financed capital expenditure on commitment *(compromisso)* and cash payments *(caix")*
- Monthly data on domestic arrears by type
- Quarterly data on official external program support (nonproject)
- Quarterly data on the execution of the public investment program (PIP) by project and source of financing
- Quarterly data on project grant and loan disbursements (HIPC and non-HIPC)
- Quarterly data on bilateral HIPC debt relief
- Latest petroleum price structures, and submission of any new pricing structures (within a week of changes).

ii. Monetary data

The BCSTP will provide the IMF staff, within three weeks from the end of each month, the monetary accounts of the BCSTP; other monetary data will be provided within six weeks after the end of each month for monthly data, within two months after the end of each quarter for quarterly data, and within two months after the end of each year for annual data. Daily data will be provided on a weekly basis no later than the Wednesday following the end of the week, and weekly data will be provided no later than two weeks after the end of such week. The BCSTP will provide:

- Daily data on exchange rates
- Daily data on interest rates
- Daily liquidity management table, including base money and currency in circulation, on a weekly basis
- Daily net international reserve position
- Weekly balance sheet data of BCSTP (in BCSTP and IMF formats)
- Monthly balance sheet data of BCSTP (in BCSTP and IMF formats)
- Monthly balance sheet data of individual deposit money banks (in BCSTP and IMF formats)
- Monthly consolidated balance sheet data of deposit money banks (in BCSTP and IMF formats)
- Monthly monetary survey (in BCSTP and IMF formats)
- Monthly central bank foreign exchange balance (*Orçamento cambial*)
- Quarterly table on banks' prudential ratios and financial soundness indicators
- Quarterly data on the BCSTP's financial position (profit and loss statement, treasury deficit, budget execution).

iii. External debt data

The Debt Management Unit at the Ministry of Planning and Finance will provide the IMF staff, within two months after the end of each month

- Monthly data on amortization and interest of external debt by creditor: scheduled, subject to debt relief or rescheduling, and paid
- Quarterly data on disbursements for foreign-financed projects and program support loans

iv. National accounts and trade statistics

The following data will be provided to the IMF staff:

- Monthly consumer price index data, will be provided by the National Institute of Statistics within one month after the end of each month
- Monthly data on imports (value and import taxes collected and arrears) and commodity export values will be provided by Customs, within two months after the end of each month
- Monthly data on petroleum shipments and consumption (volumes, CIF prices; by product).

APPENDIX II

SÃO TOMÉ AND PRÍNCIPE: RELATIONS WITH THE FUND

(As of November 30, 2006)

I. Membership Status: Joined 09/30/1977; Article XIV

II. General Resources Account:	SDR million	Percent Quota
Quota	7.40	100.00
Fund holdings of currency	7.40	100.05

III. SDR Department:	SDR million	Percent Allocation
Net cumulative allocation	0.62	100.00
Holdings	0.15	23.50

IV. Outstanding Purchases and Loans:	SDR million	Percent Quota
Poverty Reduction and Growth Facility (PRGF) arrangements	2.79	37.71

V. Financial Arrangements:

Type	Approval Date	Expiration Date	Amount Approved (SDR million)	Amount Drawn (SDR million)
PRGF	08/01/2005	07/31/2008	2.96	1.27
PRGF	04/28/2000	04/27/2003	6.66	1.90
SAF	06/02/1989	06/01/1992	2.80	0.80

VI. Projected Obligations to the Fund

(SDR million; based on current use of resources and present holdings of SDRs):

	Forthcoming				
	2006	2007	2008	2009	2010
Principal	0.10	0.38	0.38	0.38	0.29
Charges/interest	0.01	0.03	0.03	0.03	0.03
Total	0.10	0.41	0.41	0.41	0.31

VII. Implementation of HIPC Initiative:

	Enhanced Framework
Commitment of HIPC assistance	
Decision point date	12/20/00
Assistance committed (NPV terms) [1]	
Total assistance (US$ millions)	97.00
Of which: IMF assistance (SDR millions)	0.00
Completion point date	Floating
Disbursement of IMF assistance (SDR millions)	
Assistance disbursed to the member	0.00
Interim assistance	0.00
Completion point	0.00
Amount applied against member's obligations (cumulative)	0.00

VIII. Safeguards Assessments:

According to Fund policy, the Central Bank of São Tomé and Príncipe was subject to a full safeguards assessment with respect to the arrangement approved on August 1, 2005. The assessment, which was completed on August 2, 2004, found vulnerabilities in the areas of financial reporting, internal audit and internal control. Measures to strengthen the control framework and help safeguard IMF resources were proposed. Most of the recommendations have been implemented, including contracting external audit, publishing BCSTP audited financial statements, adopting International Financial Reporting Standards (IFRS), adopting a strategic plan to modernize BCSTP's internal audit.

IX. Exchange Arrangements:

The IMF classifies São Tomé and Príncipe's exchange rate regime as managed floating with no preannounced path for the exchange rate. The official exchange rate is determined daily as a weighted average of the previous day's selling rates in the commercial banks and the outcomes of central bank foreign exchange auctions. In early 2006, the multiple currency practice related to the spread between central bank buying and selling rates was eliminated, and the spread was set at 2 percent. The authorities intend to remove the exchange restriction on transfers abroad of dividends with the new Investment Code (adoption expected for end-2006). The remaining exchange restriction and multiple currency practice is related to the possibility of rationing at the auctions by the central bank, and of commercial bank rates deviating, temporarily, by more than 2 percent from the BCSTP reference rate in-between auctions. The intervention currency for the dobra is the U.S. dollar. The official selling exchange rate was Db. 13,139.8 per U.S. dollar on November 30, 2006.

X. Article IV Consultation:

The Executive Board concluded the last Article IV consultation with São Tomé and Príncipe on March 6, 2006.

XI. Financial Sector Assessment Program (FSAP), Reports on Observance of Standards and Codes (ROSCs), and Offshore Financial Center (OFC) Assessments:

None.

XII. Technical Assistance:

Nov./Dec. 2006:	LEG mission on tax codes.
Nov./Dec. 2006:	MCM mission on banking supervision.
Nov./Dec. 2006:	MFD missions on foreign exchange market and monetary operations.
August 2006:	MFD mission on banking supervision.
June 2006:	MFD mission to assess implementation of technical assistance.
April/May 2006:	STA mission on monetary and financial statistics.
February 2006:	MFD mission on monetary operations and liquidity management.
January 2006:	MFD mission on the foreign exchange market.
December 2005:	LEG/MFD mission on the exchange system.
Aug./Sept. 2005:	MFD mission on banking supervision and foreign exchange operations.
February 2005:	STA technical assistance mission on national accounts statistics.
January 2005:	MFD mission on monetary operations and liquidity management.
Dec. 2004:	STA mission to advice on compilation and reporting of monetary statistics.
Oct. 2004:	STA technical assistance mission on government finance statistics.
Sept.2004:	MFD multi-sector mission to develop foreign exchange and interbank money markets.
July–Sept. 2004:	MFD expert mission on banking supervision.
June 2004:	STA technical assistance mission on balance of payments statistics.
July 2004:	MFD expert mission on monetary operations.

June 2003: STA technical assistance mission on balance of payments statistics.

Mar. and Jun 2003: STA technical assistance missions on national accounts statistics.

March 2003 and April 2004: Visits by MFD advisors on monetary policy and banking supervision.

March 2003: STA technical assistance mission on national accounts statistics.

January 1998–December 2001: MFD advisor on the conduct of monetary policy, banking supervision, and foreign exchange management.

June 2001: MFD mission on handling of banking crisis and foreign exchange market organization.

XIII. Resident Representative:

The Fund has maintained a Resident Representative office in São Tomé and Príncipe since November 1999.

APPENDIX III

SÃO TOMÉ AND PRÍNCIPE: RELATIONS WITH THE WORLD BANK GROUP

(As of December 1, 2006)

IDA operations

1. São Tomé and Príncipe joined the World Bank and IDA in 1977. New lending was suspended between 1992 and 2000 because the country lacked an appropriate macroeconomic framework.

2. The World Bank FY06–09 country assistance strategy (CAS) was well received by the Board in June 2005. Its two principal objectives are (i) to support implementation of the PRSP and (ii) to provide timely assistance to ensure that São Tomé and Príncipe is prepared to maximize the benefits of oil revenues. Given the small size of the program, the CAS is tightly focused on activities in the oil and social sectors, public sector management, and assistance with the HIPC Initiative.

3. Despite its small project portfolio, the Bank program is relatively large for such a small country. There is a broad ESW and AAA program covering oil issues, support for PRSP implementation, assistance with achieving the HIPC completion point, and analysis of trade issues through the Trade Diagnostic Study. A PEMFAR (Public Expenditure Review, Public Finance Management Review and Procurement Review) will be delivered to the authorities by end June 2007. The Bank also supports government reforms by providing advisory services in the petroleum sector, telecommunications, and the environment. An Institutional Development Grant (IDG) was approved in early 2005 to support the government's judicial reform program. A GEF (Global Environmental Fund) was approved in late 2004 to support the drafting of a national action plan to adapt to environmental and global warming impacts. A grant was approved in May 2006 to support statistical capacity building. A PPIAF (Public-Private Infrastructure Advisory Facility) was approved in the Fall 2006 to assist with potential developments for the port.

4. Current IDA commitments for the two current projects amount to US$11.5 million, of which US$7.8 million is undisbursed. The Bank supports the health and the education sectors through its Social Sector Project of US$6.5 million, of which US$1.5 million consists of an IDA grant. The Bank supports the PRSP process, public expenditure management, and petroleum sector supervision through its Governance Capacity Building Technical Assistance Project of US$5 million. The two projects are rated marginally satisfactory; their performance is hampered by political instability, weak management, and limited absorptive capacity.

IFC operations

5. São Tomé and Príncipe is not a member of the IFC. FIAS has reviewed the country's tax system and private sector investment.

Contact persons

6. Questions may be addressed to Dorsati Madani (telephone 202-473-7925) or Rafael Munoz Moreno (telephone: 202-458-8928).

Table III.1. São Tomé and Príncipe: Statement of IDA Credits as of December 1, 2006
(Millions of U.S. dollars)

Credit Number	Fiscal Year	Purpose	IDA Commitment[1]	Undisbursed
1590	1985	Economic rehabilitation	5.0	0.0
A029	1987	Special African Facility	3.0	0.0
1825	1987	Structural adjustment credit	4.0	0.0
1830	1987	Cocoa rehabilitation credit	7.9	0.0
2038	1989	Multisector credit	5.0	0.0
2165	1990	Second structural adjustment credit	9.8	0.0
2280	1991	Multisector II credit	6.0	0.0
2325	1991	Agricultural sector	9.8	0.3
2343	1992	Health and education	11.4	0.7
3428	2000	Public resource management project	7.5	1.9
3429	2000	Public resource management technical assistance	2.5	0.0
3902	2004	Social sector support project	6.5	4.9
3993	2005	Governance Capacity Building technical assistance	5.0	2.9
	Total:		83.4	10.7
Of which: repaid			7.2	

[1]Less cancellation.

IMF-World Bank collaboration in specific areas

7. IMF and World Bank staffs collaborate on (i) macroeconomic discussions with the government; (ii) monitoring the HIPC Initiative completion point triggers; (iii) analysis and reforms in oil revenue management, the setting up of a computerized public expenditure management system, and the PRSP process; and (iv) other structural reforms, including tax reform. Table III. 2 briefly describes each area and the specific policy advice support each institution provides.

Table III.2. São Tomé and Príncipe: Areas of Bank-Fund Collaboration

Area	Description	Specialized Advice/Reforms Supported by the Fund	Specialized Advice/Reforms Supported by the Bank
HIPC completion point triggers	Regular Bank and Fund missions Elaboration of JSAN on PRSP and on PRSP First Annual Progress Report	Economic program consistent with PRGF arrangement.	Reforms in education and health sectors Judicial reform and advice on setting up tribunals of arbitration for business disputes Reform of public finance management and improved transparency of budgetary process Public expenditure review in the health sector
Oil revenue management	Regular Bank and Fund missions and Bank technical assistance missions	Advise on the use of oil proceeds consistent with Oil Revenue Management Law (ORML). Follow-up on transparency and governance issues.	Advice on the use of oil proceeds consistent with ORML Technical assistance to strengthen capacity of the country to address analysis, understanding, and management of petroleum-related topics, including, but not limited to, technical assistance: to the National Agency for Oil (ANP); for strategy on oil sector development; and on implementation of the ORML, including establishment of oversight and control committees.
Public expenditure and external debt management	Bank and Fund technical assistance and other missions	Recommendations for reform of public expenditure management systems	Analysis and advice on reform of the public finance management (PFM) system, notably assistance with the design of a fully integrated, computerized budget and public expenditure management system; and the implementation of the Commonwealth Secretariat's debt-recording management system and procurement reforms.
Other structural reforms	Bank and Fund technical assistance and supervision missions	Banking sector supervision, foreign exchange auction management, liquidity management, central bank safeguards assessment. Technical assistance on tax reform including new personal and corporate income tax codes, tax procedural codes, and investment code.	Social sector support policies and capacity building (social sector support project) Studies on the feasibility of restructuring ENASA and ENAPORT Diagnostic and Trade Integration Study (DTIS) Simplification of business registration procedures

APPENDIX IV

SÃO TOMÉ AND PRÍNCIPE: RELATIONS WITH THE AFRICAN DEVELOPMENT BANK GROUP (As of December 11, 2006)

1. São Tomé and Príncipe became a member of the African Development Bank Group in 1976. To date, the Bank Group has financed 24 operations in the country. The net commitments amount to UA 87.56 million,[1] comprising UA 86.56 million of African Development Fund (ADF) [2] and Technical Assistance Facility (TAF) resources and UA 1.00 million of Nigerian Trust Fund (NTF) resources. The sectors benefiting from AfDB Group financing are transport (26 percent), multisector [3] (22 percent), agriculture (22 percent), social sector (18 percent), and public utilities (12 percent). These operations have helped build and rehabilitate basic economic and social infrastructure (roads, airport, electricity, water, schools, health centers) and have strengthened São Tomé and Príncipe's economic and institutional capacities. The AfDB has had a national program office since 1999.

2. The AfDB has two ongoing projects; the disbursement rate was 48 percent as of December 2006. The two projects, in accordance with the PRSP, have focused on the main factors affecting poverty. The poverty reduction project contributes to improving the lives of the vulnerable population through targeted studies and analysis of poverty profiles, censuses and surveys, statistics capacity building, micro-infrastructures, and microcredit. The human resource development project will tackle cross-sectoral capacity-building by providing for training in literacy, information, and community organization, as well as specialized vocational training adapted to specific demands, particularly in the oil and tourist sectors.

3. The AfDB Group assistance strategy for 2005–09 (Country Strategy Paper 2005–09) rests on two pillars: poverty reduction in rural area and promotion of governance in public finance management. The indicative country allocation on ADF-X resources (2005–07) is UA 4.5 million in the form of grants. The first pillar will help promote and diversify the country's economic base, especially the agricultural and rural sector, and reinforce operations in the social sectors. Under this pillar, the livestock development support project-phase II (UA 4 millions) was approved in May 2006. The second pillar will support macroeconomic reforms and governance, through an institutional support project on governance and a technical assistance on the PRSP process, which will help improve public finance management and institutional capacity building to prepare the country for the forthcoming oil era. Given the considerable needs for institutional capacity building, the AfDB will finance strategic economic and sector studies, such as the Country Governance Profile; the joint

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[1] The exchange rate for December 2006 is UA 1 = US$1.51.

[2] ADF is the concessional window (or grant for ADF-X for high debt countries), on the same conditions as IDA, of the African Development Bank Group.

[3] Institutional support and structural adjustment programs.

study with the World Bank on the integrated fiduciary assessment (PER/CFAA/CPAR); the transport sector study; and the insular costs study. Furthermore, the AfDB will finance regional capacity building initiatives, within CEMAC, ECCAS, the African Portuguese-speaking countries and the small insular countries.

4. In addition, the AfDB will continue to provide the country with financial assistance through the enhanced HIPC initiative. In April 2001, the AfDB approved debt relief of US$34.20 million at NPV terms for the end of 1999. In light of the delay in the HIPC process, the AfDB plans to extend its interim debt relief period until the completion point.

Table IV.1 Ongoing Projects as of December 6, 2006

(Millions of UA) [1]

Title of Projects	Window	Commitment	Disbursement Rate
Poverty reduction	ADF	1.48	94 percent
	TAF	0.40	
Support for human resource development	ADF	3.50	1 percent
	ADF grant	0.50	
Total		*14.08*	*48 percent*

[1] Exchange rate for December 2006 is UA 1 = US$1.51.

Appendix V

São Tomé and Príncipe: Statistical Issues

Introduction

1. Although its economic data are generally adequate for surveillance, the statistical system suffers from serious financial, human, and technological resource constraints that have slowed down efforts to strengthen the system.

2. São Tomé and Príncipe began reporting monetary and balance of payments statistics for publication in the IMF's *International Financial Statistics (IFS)* in March 1998 and has participated in the Fund's General Data Dissemination System (GDDS) since April 20, 2004. The metadata and plans for improvement have not been updated since the original metadata were posted on the DSBB. Over the period 2003–06, the country has benefited from technical assistance from STA and other providers, largely under the GDDS project for Lusophone Africa.

Real sector statistics

3. Starting in the late 1990s the quality of the national accounts began to deteriorate, mainly because source data became less available and resources allocated to statistical work dwindled. Since 1998 only preliminary flash estimates of GDP at current and constant prices have been compiled, using industry coefficients and growth rate estimates.

4. Assistance in national accounts (NA) has been a priority of the GDDS Lusophone Project. The National Institute of Statistics (INE) has focused its efforts on improving source data and implementing internationally accepted classifications. Efforts are underway to compile NA aggregates in conformity with the *1993 SNA* and to help compile a quarterly production index. Estimates for 2001 and 2002 are expected to be finalized shortly and improved NA series 1996–2002 are expected to be disseminated by the end of 2006.

5. The CPI is calculated monthly and reported to AFR with a lag of one month. Since 1997 the CPI weights have been based on a three-month household survey conducted in 1995; an updated and more comprehensive household expenditure survey is needed. Current price surveys only cover the capital, although there are plans to implement regional surveys.

6. In 2003, the authorities completed, with assistance from the World Bank, the first comprehensive survey of unemployment, which provides a detailed breakdown by age, gender, and geographic location.

Government finance statistics

7. Detailed revenue and expenditure data is compiled and reported to AFR with a lag of about a month. The main areas that need to be strengthened in the data reported are (i) Ministry of Planning and Finance (MOF) monitoring of expenditures on projects financed by donors and (ii) below-the-line financing items. All project loans financed by donors are programmed in the budget, but some are executed independently. The government has asked development partners to help it record all external assistance in the budget. Recording of financing items is expected to improve as debt data management capacity is strengthened.

8. A STA government finance statistics (GFS) mission was undertaken in October 2004 to help the MOF compile and disseminate GFS for the general government in accordance with the IMF's *Government Finance Statistics Manual 2001(GFSM 2001)*.

9. The mission prepared bridge tables showing correspondence between national budget classification and *GFSM 2001* concepts and used to compile GFS for reporting to STA and AFR, as well as in MOF policy work. Given the importance of oil-related revenues, the mission also reviewed the classification of oil revenues under the Oil Revenue Management Law and made recommendations on classification of such transactions.

10. Currently no GFS are reported to STA for publication in the *Government Finance Statistics Yearbook* (*GFSY*) or the *IFS*.

Monetary and financial statistics

11. STA missions provided technical assistance on monetary statistics in December 2004 and April/May 2006. The accuracy of monetary data has improved and the lags with which the Central Bank of São Tomé and Principe (BCSTP) reports to the IMF have been reduced to two months.

12. The missions found that the BCSTP monthly trial balance sheets were adequate to compile monetary statistics in line with the *Monetary and Financial Statistics Manual (MFSM).* Although the accounting for revaluation adjustments (holding gains) falls short of recommended practices, data are available for correct reclassification of these adjustments. The plan of accounts of the other depository corporations is not adequate to derive monetary statistics consistent with the *MFSM*, particularly with regard to the sectorization of institutional units.

13. The 2006 mission noted progress in implementing the previous mission's recommendations and helped derive standardized report forms (SRFs) for reporting monetary and financial statistics. It also initiated an integrated monetary database to meet the data needs of the BCSTP, STA, and AFR. In light of recent staff turnover, the mission provided substantial on-the-job-training to compilers.

External sector statistics

14. The authorities compile exchange rates of the official exchange bureaus, commercial banks, and the parallel market. The BCSTP's official exchange rate is available on the Internet with a one-day lag.

15. There are significant weaknesses in the collection of source data related to merchandise trade. Some transactions, including certain imports related to investment, are not fully captured in the balance of payments (BoP). Monthly data on the main exports and imports are reported to AFR regularly, but unit prices and volumes of exports are only occasionally included.

16. The BCSTP compiles BoP statistics. Annual data up to and including 2002 were reported to STA in 2003 and published in the *IFS*; no data have been reported since then.

17. As part of the GDDS Lusophone project, STA launched a TA program to improve BoP compilation and dissemination. The project targeted a substantial improvement in the source data, including the response rate to the surveys, and in the methodology for compiling the BoP consistent with the *Fifth Edition of the Balance of Payments Manual*. The first mission, in June 2003, reviewed the shortcomings of reported current and financial account transactions and concluded that weaknesses were mainly due to undercoverage of several important sectors, including foreign direct investment and commercial bank reports on international transactions.

18. A follow-up mission in June 2004 found that despite efforts to implement the previous recommendations, several measures, in particular those related to improving source data, were only partially implemented, if at all. As a result, inconsistencies in the classification of BoP operations persisted and certain components continued to be largely estimated. Resource constraints, particularly with regard to qualified staff, contribute to the lack of improvement in the response rate to surveys. The mission recommended improving coordination and data sharing among data-producing agencies, intensifying contacts with survey respondents, and using alternative sources to improve source data. STA has scheduled a follow-up balance of payments statistics mission for 2007.

19. The authorities have built on previous efforts to strengthen debt data management. A new unit was created in late 2003 within the MOF. The authorities are reconciling debt records with creditors and the Commonwealth Secretariat debt recording and management system (CS-DRMS) is being operationalized.

São Tomé and Príncipe: Common Indicators Required for Surveillance (As of December 30, 2006)

	Date of latest observation	Date received	Frequency of Data[6]	Frequency of Reporting[6]	Frequency of publication[6]
Exchange rates	Dec 2006	Dec 2006	D	D	D
International reserve assets and reserve liabilities of the monetary authorities [1]	Nov 2006	Dec 2006	M	M	M
Reserve/base money	Dec 2006	Dec 2006	D	D	D
Broad money	Oct 2006	Dec 2006	M	M	M
Central bank balance sheet	Nov 2006	Dec 2006	M	M	M
Consolidated balance sheet of the banking system	Oct 2006	Dec 2006	M	M	M
Interest rates [2]	Nov 2006	Dec 2006	M	M	M
Consumer Price Index	Nov 2006	Dec 2006	M	M	M
Revenue, expenditure, balance and composition of financing [3] – general government [4]	NA	NA	NA	NA	NA
Revenue, expenditure, balance and composition of financing [3]– central government	Nov 2006	Dec 2006	M	M	M
Stocks of central government and central government-guaranteed debt [5]	Dec 2005	Mar 2006	A	I	A
External current account balance	Dec 2005	Apr 2006	A	I	A
Exports and imports of goods and services	Dec 2005	Apr 2006	A	I	A
GDP/GNP	2005	Nov 2006	A	I	A
Gross external debt	Dec 2005	Mar 2006	Q	Q	I

[1] Includes reserve asset pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially determined, including discount rates, money market rates, and rates on treasury bills, notes, and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extrabudgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); not available (NA).

Statement by the IMF Staff Representative
January 17, 2007

1. São Tomé and Príncipe has shown a strong commitment to implement the program, the response to financial slippages has overall been adequate, and progress on structural reforms in support of growth and poverty reduction has been strong. Growth in 2006 has been solid, and inflation, after flaring up in the first half of the year, has shown signs of receding. However, São Tomé and Príncipe remains vulnerable to domestic and external shocks.

2. While the financial program performance was unsatisfactory in the first half of 2006, the authorities took remedial measures that have since brought the program broadly back on track. The increased tax collections and containment of expenditures since May have largely offset overruns during the period leading to the elections and the domestic primary deficit target for 2006 should be within reach. However, propoor spending has been below expectations.

3. The primary deficit target for 2007 shows significant efforts to create room for increased propoor spending, while taking into account delays in oil bonus receipts. It will be critical to reduce nonessential spending and continue implementing the tax reform. Propoor spending should be further boosted by prospective HIPC relief and MDRI resources following the completion point.

4. The central bank's current prudent monetary policies are broadly appropriate to significantly bring down inflation. In this regard, the central bank's recent efforts to activate its monetary and foreign exchange policy instruments are noteworthy, in particular, the resumption of regular foreign exchange auctions and the issuance of certificates of deposits. It is important that the central bank adhere strictly to its base money and net international reserves targets and move promptly to mop up liquidity as needed.

5. São Tomé and Príncipe's managed floating exchange rate system has helped cushion against external shocks as the exchange rate remains largely market determined. The central bank should be able to gradually eliminate the remaining exchange restriction and multiple currency practice for external current transactions.

6. Structural reforms have been progressing well, especially with the steps to strengthen public financial management, lay the basis for tax reform, and combat money laundering and the financing of terrorism. Full implementation of the new public financial management system will be essential for monitoring the spending and use of debt relief resources for poverty reduction. Further improvements in the environment for private sector activity are key for sustained growth, and the reforms of the tax system and the energy and financial sectors should be pursued.

INTERNATIONAL MONETARY FUND
EXTERNAL RELATIONS DEPARTMENT

Press Release No. 07/5
FOR IMMEDIATE RELEASE
January 17, 2007

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Completes Third Review of São Tomé and Príncipe's Three-Year PRGF Arrangement and Approves US$600,000 Disbursement

The Executive Board of the International Monetary Fund (IMF) has completed the third review of São Tomé and Príncipe's economic performance under a three-year Poverty Reduction and Growth Facility (PRGF) arrangement. The completion of the review enables the release of an amount equivalent to SDR 0.4 million (about US$600,000), which would bring total disbursements under the arrangement to SDR 1.7 million (about US$2.5 million).

In completing the review, the Executive Board approved waivers for the nonobservance of several end-June 2006 performance criteria. The Board also approved the modification or deletion of certain end-December 2006 performance criteria.

The Executive Board approved the three-year arrangement on August 1, 2005 (see Press Release No. 05/187), for a total amount of SDR 2.96 million (about US$4.26 million) to support the government's economic program for 2005–07.

In commenting on the Executive Board's discussion on São Tomé and Príncipe, Mr. Murilo Portugal, Deputy Managing Director and Acting Chair, stated:

"São Tomé and Príncipe has shown a renewed strong commitment to program implementation with an adequate response to financial slippages and strong progress on structural reforms in support of growth and poverty reduction. The remedial measures that the authorities have put in place have brought their program broadly back on track. The increased tax collections and the containment of expenditures have largely offset election-related expenditure overruns. However, pro-poor spending remains below expectations.

"The authorities are committed to putting in place substantive fiscal measures to create room for increased pro-poor spending. For this purpose, they will focus on reducing nonessential spending and implementing the tax reform. Pro-poor spending should be further boosted by prospective HIPC and MDRI debt relief.

"The central bank is making a more proactive use of monetary policy instruments to help reduce inflation. The resumption of regular foreign exchange auctions, the issuance of certificates of deposits, and the commitment to adhering strictly to its base money and net international reserves targets are commendable. It will be important to act promptly to mop up liquidity as needed.

"São Tomé and Príncipe's managed floating exchange rate system has helped cushion against external shocks as the exchange rate remains largely market determined. The central bank will gradually eliminate the remaining exchange restriction and multiple currency practice for external current transactions.

"Structural reforms are progressing well, especially with the steps taken to strengthen public financial management, lay the basis for tax reform, and enhance financial sector supervision. Full implementation of the new public financial management system will enable accurate expenditure monitoring, while further reforms of the tax system and the energy and water sectors, and improvements in the environment for private sector activity will lay the foundation for sustained growth, employment, and poverty alleviation," Mr. Portugal said.

Statement by Mr. Laurean W. Rutayisire, Executive Director for the Democratic Republic of São Tomé and Príncipe January 17, 2007

On behalf on my Saotomean authorities, I would like to express my deep appreciation to Management and Staff for their continued policy advice and support to São Tomé and Príncipe. Discussions held with Staff in Sao Tome in June and November 2006 have been very instrumental in strengthening policy design and implementation in the second part of the year. In a meeting with the Managing Director held last week in Libreville, Gabon, at the occasion of the inauguration of the Regional Technical Assistance Center, AFRITAC Center, my authorities reaffirmed their commitment to the achievement of the program objectives and their program ownership. They are determined to press ahead with their reform agenda, in order to create the conditions for low inflation and sustained growth, which is essential for poverty reduction. However, they also concur with the view that the successful implementation of the reforms will depend on the need to address the administrative and institutional capacity constraints facing the country. In this regard, they hope that they can continue to count on the support and technical assistance of the international community to help them advance towards the MDGs.

Under the program, five of the six structural benchmarks through September 2006 were met, and strong remedial actions were taken on the five quantitative performance criteria (PC) for end-June 2006 that were missed by small margins. My authorities regard the successful completion of the third review as merit for reaching the completion point under the HIPC Initiative and request the Board's consideration in this regard. They consider—a view also shared by staff—that significant progress was made to implement all completion point triggers agreed upon at the decision point, including the implementation of the required health and education measures, the putting in place of institutional mechanisms to ensure efficient and transparent use of HIPC interim debt relief, the increase in transparency and accountability in the management of public resources, and the establishment of arbitration tribunals. They would also like to bring to the Board's attention that they have maintained a constructive dialogue with all the country's creditors and has contacted the Paris Club creditors with a view to concluding bilateral agreements under the September 2005 Paris Club terms of reference. They have also signed agreements with Germany and France, and the signature process with Spain is advanced. My authorities are resolved to ensure debt sustainability. To this effect, they are putting in place a debt recording and management system obtained from the Commonwealth Secretariat (CS-DRMS).

My authorities request waivers for the nonobservance of the end-June 2006 performance criteria for domestic primary balance, domestic primary spending, and net domestic financing of the government. These deviations are mainly due to higher spending related to the elections, and the Government has since then taken revenue and expenditure measures as well as monetary policy measures to broadly safeguard the financial targets for end-2006. The Government also requests waivers for the nonobservance of the end-June 2006 performance criteria on net international reserves and net domestic assets of the Central Bank of São Tomé and Príncipe which was mostly due to the delay in the receipt of oil signature bonuses.

Given that the higher inflation and election spending needs have required a revision of the government's fiscal program for 2006, they request modification of the targets for four quantitative performance criteria for end-December 2006 and deletion of the performance criterion for domestic primary spending. Furthermore, the Government requests deletion of the structural performance criterion on the implementation of the public financial management system (SAFE) on the understanding that it will be established in due course as a structural performance criterion for end-December 2007. The original target of fully implementing the SAFE by end-2006 was not met because agreement with a key donor and technical preparation took longer than expected.

I. Recent Developments

Economic activity in 2006 has been buoyant thanks to higher foreign direct investments in the oil and tourism sectors. Growth is expected to reach 8 percent in 2006, well above the 5.5 percent projection made at the time of the second review under PRGF. However, inflation has been higher than projected on account of various factors, including temporary food shortages, higher oil product prices, large capital inflows and unforeseen election-related spending. It reached a peak of 26 percent in August before receding to 23 percent at end-November 2006, thanks to continued sound policy implementation in the second part of 2006.

Progress was also made towards strengthening democratic institutions essential for participative implementation of appropriate macroeconomic and structural reforms programs for poverty reduction. The country held successively parliamentary, presidential, and local elections from March to July 2006. These elections further strengthened democratic institutions and confirmed São Tomé and Príncipe's well-known democratic culture. A new cabinet was appointed in April 2006 which reaffirmed its strong commitment to implement the Fund-supported program and reach the HIPC completion point. The improved economic performance at end-December 2006 demonstrates this commitment. It is worth indicating that although President Fradique de Menezes and his coalition—who won the three elections—has only a relative majority at the National Assembly, all political parties reiterated their strong support to the government's development and poverty reduction program. The National Assembly's passing of several laws is an evidence of this political consensus.

Fiscal Sector

Fiscal-related reforms advanced significantly with the strengthening of the Inspectorate General of Finance and the submission to and the adoption by the National Assembly of several direct tax and customs reform draft laws aimed at improving incentives, reducing distortions, lowering rates and enlarging the tax base. The authorities made good progress in preparing the integrated public financial management system for budget execution (SAFE), with notably the submission to the National Assembly of the organic public finance law and the preparation of a new budget nomenclature. However, as indicated above, the implementation of the integrated public financial management system for budget execution (SAFE) is now expected for end-2007 instead of end-2006. Nevertheless, the 2007 budget recently adopted, which is consistent with the program, will be implemented with a pilot public financial management program (SAFINHO) using the new budget classification. The authorities are aware that propoor spending is still low. They are committed to containing wages and reducing nonwage nonessential spending in order to create the fiscal space for increased propoor spending.

Through June 2006, revenue collection was better than programmed thanks to more buoyant import and domestic indirect tax receipts. Nevertheless, fiscal performance deviated from the program path owing mainly to expenditure overruns related to the elections and the need to meet unforeseen needs beyond the authorities' control, including advances by the treasury for projects, pending financing by donors. But during mid-year, several measures were executed to bring the program back on track. These involved expenditure and revenue measures, including the increase in the import reference prices and the increase in petroleum prices in May 2006. In addition, action plans to recover corporate, personal income and petroleum indirect tax arrears have been implemented. However, the receipts of oil bonuses for Block 2–4 did not materialize as expected in 2006, thus complicating the execution of the budget. As a result, domestic primary deficit is estimated to remain within the program target of 15 ½ percent of GDP, after deviating by 2 percent from the end-June program target.

Monetary Policy and Exchange Rate Policies

Developments in the real sector and fiscal sector translated in monetary aggregates—notably net international reserves (NIR), credit to the government and private foreign currency deposits– growing faster than programmed early in 2006 and higher inflation. Policy response from the Central Bank of São Tomé and Príncipe (BCSTP) consisted in successive increases of the reference interest rate from 17.2 percent at end-2005 to 28 percent in September 2006, in order to maintain a positive real interest rate. Minimum reserves requirement was also increased. However, these measures had a limited effect in mopping up excessive liquidity in the economy and reducing monetary aggregates. In December 2006, with a view to further absorbing liquidity and reducing inflation, the BCSTP decided to activate its instrument of certificates deposits (CDs). More recently, the BCSTP resumed its foreign exchange auction system while keeping direct sales to the abovementioned purposes. In addition, the National Assembly adopted the anti-money laundering law.

Structural Reforms

Reform implementation accelerated in the second semester to make up for the delays that occurred previously. In particular, the arbitration law has been promulgated and an arbitration center has been set up at the Chamber of Commerce in mid-December 2006. These two measures mark the observance of the last completion point structural trigger. In addition, a new investment code, which provides equal treatment for domestic and foreign investors and eliminates exchange restrictions on transfers of dividends abroad, has been recently adopted by the National Assembly. As regards public enterprises, studies on the electrical sector and the restructuring of the port and airport have been completed.

II. Financial Policies for 2007

São Tomé and Príncipe remains a low-income country, still facing daunting challenges, including restoring macroeconomic stability while addressing growing pressing social needs in anticipation of both the upcoming oil era, beginning hopefully from 2012. During the meeting with the Managing Director last week, my authorities reiterated their commitment to macroeconomic stability and economic reforms with a view to better preparing the country to oil era. To this end, the program for 2007 seeks to pursue policy stance adopted since May 2006 with fiscal consolidation and inflation reduction as primary objectives. My authorities are particularly aware of the need to use oil bonuses prudently, as the potential oil reserves in awarded oil blocks are yet to be ascertained.

More specifically, **fiscal policy** as reflected in the 2007 budget aims at reducing domestic primary deficit by 2.5 percent of GDP. Fiscal consolidation will be achieved essentially by containing non essential spending and the wage bill (relative to GDP) through a stricter application of administrative measures decided last year. At the same time, my authorities intend to increase pro-poor spending by approximately the same amount (2.7 percent of GDP) through a prudent use of prospective oil bonuses and debt relief resources, consistently with the PRSP, the Priority Actions Program (PAP) and the Oil Revenue Management Law (ORML). On the revenue side, the impact of the tax and customs reforms will be broadly neutral in 2007, reflecting the gradual adoption of the procedural codes.

As regard fiscal-related structural reforms, the public financial management will be further strengthened with the progressive implementation of SAFE which as indicated above will be fully operational by end-2007 for the execution of the 2008 budget. My authorities are particularly concerned about the growing informal sector and accordingly they will conduct a study on indirect taxation in order to review the current tax structure and expand the tax base, with the support of international partners. On oil-related issues, it is my authorities' intention to seek further clarification from the Joint Ministerial Committee (JMC) on the use of its important contribution (US$ 3.6 million) to the Joint Development Authority (JDA). A revised structure of the petroleum prices with fewer exemptions will be introduced by mid- March 2007, with a moderate increase in pump prices if needed.

Monetary policy for 2007 seeks to reduce the 12-month inflation to the 10–15 percent range by the end of 2007 from a level of more than 20 percent in 2006. Although this objective may appear ambitious, my authorities believe that it could be achieved through a stricter adherence to the base money target and active use of monetary and foreign exchange instruments, consistent with the NIR target, while avoiding excessive fluctuations in exchange rate and taking into account the central bank's liquidity position. The central bank will continue to strengthen its operations with a view to improving its liquidity position and increasing transparency. This will be complemented by a more active communication strategy on its operations. My authorities are particularly thankful to the Fund for the technical assistance in strengthening the central bank's instruments and technical capacities towards the achievement of its monetary objectives.

In their efforts to strengthen the **financial sector,** the Saotomean monetary authorities intend to further enhance banking supervision, implement the anti-money laundering law, and improve the internal management at the central bank in line with the IMF's safeguards assessment conducted in 2004. Also in line with the safeguards assessment, the central bank intends to publish the 2005 audited financial statements and adopt investment guidelines for international reserves by January 2007. In addition, it will issue new prudential regulations on credit classification, liquidity, transactions with related parties, and limits on net open foreign currency positions by end-June 2007. A regular system for reporting prudential ratios to IMF staff has now been established. Following the adoption by the National Assembly of the draft anti-money laundering law, the central bank intends to adopt regulations on the creation of a Central Risk Unit within the central bank.

Other **structural reforms** will focus on increasing transparency in the oil sector. The government will continue the implementation of the institutional framework for the oil revenue management, as provided for in the ORML. In addition, the authorities will proceed with the implementation of the requirements for the participation in the EITI as expressed at the third EITI conference in Oslo in October 2006. My authorities believe that structural reforms covering taxation, investment code, the energy sector and banking supervision are improving the business environment and hence should promote the development of the private sector.

Conclusion

As committed at the time of staff mission in June 2006, my authorities took strong corrective actions to bring the program back on track. They have demonstrated a strong resolve to advance structural reforms with a significant number of laws passed in the fiscal, financial and governance areas. Through these reforms, they are committed to create the conditions conducive to stronger and sustained growth. They are also determined to continue to work closely with their partners to achieve the goals of sustained growth and poverty alleviation and to strengthen capacity building. In light of these achievements, my authorities request Board approval of the completion of the third review under the PRGF, and reaching the HIPC completion point.