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Gabon: Letter of Transmittal and Memorandum of Economic and Financial Policies

June 21, 2005

The following item is a Memorandum of Economic and Financial Policies of the government of Gabon, which describes the policies that Gabon intends to implement in the context of its request for financial support from the IMF. The document, which is the property of Gabon, is being made available on the IMF website by agreement with the member as a service to users of the [IMF](#) website.

Libreville, June 21, 2005

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

Mr. de Rato:

The Government of Gabon has held discussions with Fund staff in the context of the fourth review of the program supported by the 14-month Stand-By Arrangement approved in May 2004. The attached Memorandum on Economic and Financial Policies reviews macroeconomic developments and the implementation of structural policies in the first quarter of 2005 and describes the government's economic policies for the remainder of 2005. Gabon's economic performance has continued to be satisfactory, all end-March performance criteria were met, and we intend to continue to pursue prudent macroeconomic policies for the remainder of the year. Accordingly, we hereby request completion of the fourth review under the SBA. We intend to continue to treat the arrangement as precautionary.

Sincerely yours,

/s/

Paul Toungui
Minister of State, Minister of Economy, Finance,
Budget, and Privatization

Attachment: Memorandum of Economic and Financial Policies

Memorandum of Economic and Financial Policies of the Government of Gabon

I. RECENT ECONOMIC DEVELOPMENTS AND PROSPECTS

1. **GDP growth is estimated to have reached 1½ percent in 2004.** Non-oil growth picked up slightly to 2¼ percent, thanks mainly to rising output in manganese mining; nevertheless, a decline in oil sector activity in 2004 represented a drag on overall growth performance. **Inflation** fell to ½ percent in 2004, reflecting wage moderation and the monetary discipline imposed by the exchange rate regime, and remained subdued in the first quarter of 2005. As a result, the real exchange rate depreciated slightly in 2004 and early 2005, and competitiveness remains satisfactory. The external position remains strong, with the current account surplus reaching 10½ percent of GDP in 2004 and Gabon's contribution to the BEAC's external assets more than doubling.
2. **The fiscal stance remained tight in 2004.** Buoyant oil prices contributed to an overall budget surplus of 7½ percent of GDP. Oil windfall revenue was used primarily to reduce domestic and external debt and, to a lesser extent, increase government deposits in the Fund for Future Generations. At the same time, the non-oil primary deficit fell by ½ percentage point to 7¾ percent of non-oil GDP, reflecting both an improvement in non-oil revenue collection and expenditure restraint, notably on wages and salaries.
3. **The economy strengthened in the first quarter of 2005.** While oil production remained broadly stable, strong global demand for steel buoyed Gabon's production of manganese, which rose by more than 10 percent over the first quarter of 2004, and timber production and exports recovered sharply from their depressed levels of 2004. Rising output of construction materials and a robust increase in the consumption of energy provide additional evidence that a broad-based economic recovery is underway. The strength in the economy was reflected in good non-oil revenue performance during the first quarter, which together with continued expenditure control has allowed the government to meet its fiscal objectives and observe the performance criteria on the primary surplus and net credit to the Government for end-March 2005 under the Stand-By Arrangement.
4. Since the debt rescheduling agreement concluded with Paris Club creditors on June 11, 2004, negotiations for bilateral agreements have been completed with all creditors, except with Brazil where an agreement has been reached and final signature is pending. In view of our strong external position, we are not requesting any rescheduling of maturities falling due beyond end-June 2005. With respect to its debt to non-Paris Club bilateral creditors, Gabon continues to pursue negotiations with Saudi Arabia, China, Libya, and South Korea. An agreement with the London Club of commercial creditors has been reached and is expected to be signed by mid-July 2005.

II. POLICIES FOR THE REMAINDER OF 2005

5. **The economic outlook for 2005 is positive.** We expect oil production to remain at its 2004 level, while prices will remain favorable despite the deeper discount applied to Gabonese oil. In the non-oil sector, we expect manganese and timber exports to remain strong and the recovery in construction and agroindustry to continue. As a result, we expect non-oil GDP growth to accelerate to at least 3 percent in 2005. Meanwhile, inflation is not expected to exceed 1 percent and the external position is expected to remain strong, with the current account surplus rising to 12½ percent of GDP and a further build-up of exchange reserves. Accordingly, we expect that the external public debt/GDP ratio will fall from 50 percent at end-2004 to 42 percent by end-2005.

6. **Fiscal policy for the remainder of the year will adhere to the 2005 budget law.** We expect non-oil revenue to increase as anticipated and reach the target of 25.2 percent of non-oil GDP, a one percentage point increase over 2004. Oil revenues, on the other hand, are likely to be slightly below target as a result of the widening discount for Gabonese oil this year. On the expenditure side, we intend to maintain strict control of civil service wages through a series of measures aimed at ensuring that the 2005 wage bill remains unchanged in nominal terms over the previous year. However, there are two areas in which expenditures will exceed planned levels and we intend to adopt a supplementary budget, probably toward the end of the third quarter, to incorporate these additional expenditures. First, the financial situation of Air Gabon has reached critical proportions and we have decided to proceed with its liquidation (see paragraph 10). This will, however, have important financial implications for the government: to ensure operations until liquidation takes place; to meet legal redundancy payments to Air Gabon staff; and to settle Air Gabon's outstanding payment arrears after a detailed audit and their integration in public debt. Provisional estimates, which will be refined before end-July 2005, suggest that the total gross cost could reach CFAF 43-53 billion (1-1.¼ percent of GDP), not including any proceeds from asset sales. Second, after the PRSP has been finalized (expected in August 2005 – see paragraph 17), we intend to identify urgent financing needs aimed directly at poverty reduction. We intend to address these needs primarily in the context of the 2006 budget; nevertheless, there could be some expenditures in 2005, which however would not exceed CFAF 5 billion. As a result, we now expect the non-oil primary deficit to fall at a slower pace than originally envisaged, reaching about 6¾ percent of non-oil GDP in 2005.

7. **Fiscal policy over the medium-term will aim at further steady consolidation.** In view of our finite oil resources and associated government revenue it will be necessary to maintain a strong non-oil revenue effort and continue to streamline expenditures, particularly on the wage bill. At the same time, we intend to manage oil revenue prudently and saving the full amount of oil-related revenue resulting from oil prices in excess of US\$35 per barrel of Brent, which will allow us to maintain the pace of reducing the level of public debt to more manageable levels. To this end, we intend to reduce the non-oil primary deficit as a ratio of non-oil GDP by roughly 1 percentage point per annum over the next three years. However,

this objective could be adjusted downward as a result of well-defined financing needs identified in the PRSP, provided that the fiscal adjustment remains consistent with maintaining public debt sustainability.

8. **Reforms of our fiscal management systems are underway to strengthen both the revenue basis and improve expenditure control.** The Large-Tax Payer Unit (LTU) will assist the Tax Directorate in the assessment of a number of large cases this year before becoming fully operational in 2006. Significant progress has been made this year in land titling, which has strengthened the finances of the local authorities by broadening their property tax base. And improved cash management at the Treasury has allowed us to settle government bills in an orderly manner and reduce the Treasury float significantly. But an important agenda remains to improve public expenditure management. In preparation of the 2006 budget law over the coming months, we intend to improve the coordination between the current and the investment budgets by reintroducing joint budgetary conferences and harmonize the technical preparation of the budgets between the Ministry of Finance and the Ministry of Planning. We also intend to elevate the status of the 3-year Public Investment Program, which currently is largely indicative, to become a more binding framework for public investment spending. Finally, we intend to bring to a rapid conclusion the work in introducing a functional budget classification, which will allow for a significant improvement in budgetary management, notably in the execution of the 2006 budget.

9. **Comprehensive structural reforms are critical to diversifying the economy and improving Gabon's economic growth prospects.** To that end, the Government remains committed to the privatization of certain public enterprises, to improving the investment climate in Gabon, to reinforce the financial sector as a foundation for private-sector led growth, and to reform the sector of natural resources, which will be critical to Gabon's future prosperity and growth.

10. **The Government's privatization program is underway.** The Government has reached a cross-debt cancellation agreement with Gabon Telecom and private mobile telephone operators to streamline Gabon Telecom's balance sheet. Over the coming weeks we will eliminate the remaining uncertainties in GT's balance sheet, including the status of its assets, so that it can be rapidly brought to tender. We have established a timetable that aims at divesting a majority stake in GT by September 2005. Concerning Air Gabon, we intend to proceed rapidly with its liquidation. Redundancy procedures for its personnel have been initiated and should be concluded by October 2005 at the latest. By end-July we expect to have completed the audit of Air Gabon's outstanding debts, as well as its claims, which will allow us to quantify more precisely the costs of the liquidation. In the meantime, discussions with potential buyers will start with the objective of creating a new airline company with a majority private sector participation, which would be managed on a commercial basis. Detailed documentation has been sent to a limited number of potential investors with a response deadline of July 18 and we expect to choose the strategic partner by end-July 2005. The new company is expected to become operational in early 2006.

11. **The Government is preparing an action plan to improve the investment climate in Gabon.** Following the report by the FIAS and the work shop held with the private sector last February, the Government is finalizing a program that aims to tackle the main problems identified by the private sector: (i) improve access to financing for SMEs; (ii) reduce factor costs, particularly the very high costs of port and transport operations; (iii) restructure the Investment Promotion Agency with the aim of streamlining the process of establishing a new business; (iv) simplify administrative procedures and improve the environment for foreign investors; (v) finalize the new tax code and effectively eliminate parafiscal taxes; (vi) boost the supply of skilled labor by modernizing the vocational training centers; (vii) strengthen the administrative environment by improving the functioning of the courts and encouraging a wider dissemination of the new company law of OHADA; and (viii) facilitate investors' access to real estate.

12. **Financial sector reforms are a key element to boosting private sector development in Gabon.** Improved access to credit is particularly important for small and medium-sized enterprises. As a first step, we intend to align the tax treatment of banks' provisions with the norms of the COBAC that apply throughout the CEMAC zone, followed by further regulatory and legal harmonization. Regarding the promotion of microfinance, a government working group is developing a strategy, which will focus initially on capacity building.

13. **The government has launched a major reform of the natural resources sector, beginning with the forestry sector.** The monopoly of the timber marketing board (SNBG) has been lifted effective January 1, 2006, and work is underway to define the role of a down-sized SNBG. The government has initiated a policy of transparency in the forestry sector: a comprehensive list of holders of forest permits was published in February and the Government announced that all holders that do not clear their arrears or agree to a well-defined repayment schedule, will be subject to the seizure of their permits. The first seizures will take place in August 2005.

14. **The Government remains committed to strengthening governance and transparency aimed at improving the management of public resources and boosting private sector development.** The National Commission Against Illicit Enrichment is making satisfactory progress and a large number of civil servants have submitted their asset declarations. In the public sector, the audit of the arrears of the Road Maintenance Fund and of the expenditures related to the annual independence celebrations (fêtes tournantes), are expected to be finished by end-June and will be published on the web site of the Finance Ministry. The lessons from these audits will be taken into account in the preparation of the 2006 budget and the establishment of a new road maintenance fund. While ensuring full and smooth replenishment of the new road fund so that it can provide properly for the maintenance of Gabon's road network, the new procedures will ensure that the management of the fund continues to respect public procurement and accounting rules, and its full and timely integration in all fiscal reporting.

15. **Transparency is being further improved through Gabon's participation in the Extractive Industries Transparency Initiative (EITI).** A first meeting of the stakeholders group, comprising the government, the oil companies, and civil society is scheduled for July 2005. On this occasion, the government will present an action plan aimed at meeting the EITI principles by September 2005. The stakeholders group will define the reporting template for the financial flows between the government and the private sector; the oil companies will have their payments audited; the Supreme Audit Office will certify government revenues; and an independent auditor will verify the aggregation of oil company data and their reconciliation with government revenues. The government intends to establish a web site to ensure the transparency of this information and will publish the audit of the first reconciliation by end-September 2005. We expect that independent certifications will be done on at least a semi-annual basis. Gabon intends to extend the initiative to the mining sector in 2006.

16. **The Government is also committed to improving its data dissemination practices and, over the medium term, strengthen the quality of its economic statistics.** A new Statistical Law has reached an advanced stage of dissemination and is expected to be adopted by end-2005. In the meantime, the Government intends to update the information contained in its GDDS page by end-June 2005 and formulate an action plan by end-September to improve the dissemination of statistical information that is currently prepared but not systematically published.

17. **Work on the Poverty Reduction Strategy Paper (PRSP) is making good progress and we still expect it to be completed by August 2005.** The quick poverty survey (questionnaire on core welfare indicators—CWIQ) is currently being conducted and will be completed by end-June. Its evaluation, including an update of poverty indicators as well as other social indicators, will be available by end-July. Consultations with civil society and the private sector are also underway. The government intends to use this work, together with the results of the public expenditure review scheduled for June-July, to prioritize the three-year public investment program and harmonize it with the 2006 budget.

Table 1. Gabon: Quantitative Performance Criteria and Indicative Targets Under the Stand-By Arrangement, 2004-05
(In billions of CFA francs; end-period data; cumulative flows from January 1st) 1/

	2004				2005				Indicative
	Mar.	Jun.	Sept.	Dec.	Mar.	Jun.	Sept.	Dec.	
	Prel.	Prel.	Prel.	Prel.	Prog.	Deviation	Deviation	Indicative	
Performance criteria									
Ceiling on the net claims of the banking system on the central government 2/	-22.4	-61.4	-48.5	-86.0	-20.2	7.6	-59.3	-53.3	-150.7
Adjusted target 2/					25.2				
Ceiling on the contracting or guaranteeing of new nonconcessional external debt with maturity of over 1 year by the central government 3/	2.5	9.5	13.4	59.9	32.0	5.9	32.0	32.0	32.0
Ceiling on outstanding stock of new nonconcessional external debt with original maturity of one year or less owed or guaranteed by the central government 4/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Ceiling on the accumulation of external payments arrears by the central government 5/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Stock of arrears on domestic debt of the central government 6/	14.1	5.5	5.5	0.0	0.0	0.0	0.0	0.0	0.0
Adjusted target 6/	0.0	0.0	0.0	1.9	0.0	0.0	0.0	0.0	0.0
Floor on the primary fiscal balance of the central government, excl. grants and foreign-financed investment (on a payments order basis) 7/	116.6	233.6	339.6	453.0	137.2	129.6	290.7	428.5	589.0
Adjusted target 7/					111.3				
Indicative targets:									
Floor on non-oil central government revenue	124.5	245.3	362.0	511.5	116.2	123.9	270.9	384.3	556.2
Ceiling on the central government wage bill on a payments order basis	55.4	110.1	168.3	226.3	56.2	55.1	112.0	169.8	226.0
Ceiling on total noninterest domestic expenditure of the central government, on a payments order basis 8/	154.5	296.2	462.0	658.5	160.5	149.9	335.2	488.2	677.1
Floor on current expenditure for the sectors of education, health and social assistance.	7.2	17.2	25.8	35.2	8.0	8.4	20.0	30.0	40.0
Floor on the net reduction of unpaid payments orders at the treasury 9/			0.0	-67.4	-39.3	-58.8	-84.3	-85.9	-90.1
Memorandum items:									
Nonproject external financing disbursements (excluding IMF)	0.0	0.0	0.0	44.2	0.8	0.0	2.0	3.8	5.0
External debt service due (excluding IMF)	83.6	147.4	244.2	327.6	96.3	85.7	149.4	243.8	302.7
Domestic debt service due	9.6	36.7	57.5	83.4	17.3	36.8	62.9	84.2	100.8
Oil revenue	146.6	284.5	439.7	600.0	181.5	155.6	355.0	532.5	709.9
Rescheduling of external debt 10/	0.0	395.4	419.0	425.4	46.4	45.2	75.3	75.3	76.6
Privatization proceeds	0.0	0.0	0.0	1.7	0.0	0.0	0.0	0.0	18.2

Sources: Gabonese authorities; and Fund staff estimates and projections.

- 1/ Indicative targets for end-March 2004, end-June, end-September, and end-December 2005. Targets for end-June, end-September, end-December 2004, and end-March 2005 are performance criteria under the SBA.
- 2/ The performance criterion will be adjusted upward/downward for any lower/higher oil revenues, larger/lower payment of external debt service (net of nonproject external financing disbursements), larger/smaller net reductions in domestic arrears, and smaller/larger privatization proceeds, relative to program targets. The performance criterion will be adjusted downward for unprogrammed rescheduling/deterioration on domestic debt.
- 3/ 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 by the IMF Executive Board on August 24, 2000, but also to commitments contracted or guaranteed for which value has not been received. Excluded from this performance criterion are rescheduling arrangements and purchases from the Fund. For purposes of this performance criterion, the term "nonconcessional" means that the debt has a grant element of less than 35 percent, calculated on the basis of currency-specific discount rates that are based on the OECD commercial interest reference rates (CIRRs).
- 4/ Excluded from this performance criterion are rescheduling arrangements, purchases from the Fund, and normal import-related credits.
- 5/ The nonaccumulation of new external payments arrears will constitute a continuous performance criterion.
- 6/ As defined in paragraph 10 of the Technical Memorandum of Understanding (TMU). The ceiling on bank financing will be adjusted downward/upward for unprogrammed rescheduling/deferrals.
- 7/ The performance criterion on the primary fiscal balance will be adjusted upward/downward for any higher/lower-than-programmed oil revenue. For end-December 2004, the original program target has been revised to reflect the higher oil revenue and the upward adjustment in current spending by CFAF 1 billion.
- 8/ Noninterest spending excluding foreign-financed investment.
- 9/ Including the reduction of arrears on the wage bill and the payment of compensations for social violence.
- 10/ These amounts represent rescheduled end-April 2004 stock of arrears and the obligations falling due during May-December 2004 and January-June 2005, in line with the Paris Club agreed minutes of June 11, 2004.
- 11/ As revised in EBS/04/174.

Table 2. Gabon: Structural Performance Criteria and Benchmarks
Under the Stand-By Arrangement, 2004–05

Measures	Implementation Period	Status of Implementation
Structural performance criteria		
<i>Fiscal policy/Development of the private sector</i>		
Adoption of a decree establishing the large enterprise tax unit within the tax administration department, which covers all enterprises with annual turnover over CFAF 1 billion.	End-September 2004	Met.
<i>Forestry sector</i>		
Adoption of time-bound action plan to streamline SNBG, on the basis of World Bank-financed study.	End-November 2004	Met in December 2004.
Structural benchmarks		
<i>Civil service reform</i>		
Harmonization of the civil service and payroll rosters, based on the computerized civil service management system (ANITA).	End-December 2004	Met with the introduction of a unified personnel roster (<i>fichier unique de référence – FUR</i>)
Adoption of implementing decrees on the new wage structure and promotion system, on the basis of the new law on the general civil service statute.	End-December 2004	Not met. Draft law approved by parliament in January 2005. Implementing decrees delayed until the law is assessed.
<i>Fiscal policy</i>		
Integration in the 2005 government budget of all special funds.	End-December 2004	Not met. Only accounts of the National Housing Fund and the local authorities will be integrated through a supplementary budget in 2005.

Table 2. Gabon: Structural Performance Criteria and Benchmarks
Under the Stand-By Arrangement, 2004–05 (continued)

Measures	Implementation Period	Status of Implementation
No granting of exemptions to any company beyond those already provided for under the mining, forestry, and investment code, and no renewal of existing exemptions.	Continuous benchmark	Not met. A convention signed with a leading manganese company extends existing exemptions.
Completion of assessment of stock of wage arrears.	End-September 2004	Met.
Finalization of taxable base for local real estate taxation for Libreville and Port-Gentil.	End-December 2004	Met.
Establishment of detailed budgetary appropriations for investment expenditures, according to the budgetary classification, in the 2005 Budget Law submitted to parliament.	End-December 2004	Met.
Entry into effectiveness of budgetary credits for the 2005 budget before end-February 2005.	End-February 2005	Met.
Establishment of a performance contract with the National Social Guarantee Fund, CNGS.	End-September 2004	Met in mid-November, 2004.
Issuance of interministerial report on local authorities' finances.	End-October 2004	Met.

Table 2. Gabon: Structural Performance Criteria and Benchmarks
Under the Stand-By Arrangement, 2004–05 (continued)

Measures	Implementation Period	Status of Implementation
Preparation of a study with recommendations to prioritize the university scholarship system.	End-October 2004	Met.
Adoption of an action plan based on additional recommendations by a commission chaired by the Deputy Prime Minister. ¹	End-May 2005	Not met. Draft action plan still in preparation.
<i>Good governance</i>		
Preparation of the first report on the operations of the Commission Against Illicit Enrichment.	End-December 2004	Met.
Inclusion in the 2005 budget of an adequate operational budget for the National Commission Against Illicit Enrichment.	End-December 2004	Met.
<i>Development of the private sector</i>		
Adoption of the implementation regulations for the mining code.	End-December 2004	Not met. Delayed to the second half of 2005.
No recourse to price control measures, and no widening of the list of products subject to the price surveillance regime at end-December 2003.	Continuous benchmark.	Met.

Table 2. Gabon: Structural Performance Criteria and Benchmarks
Under Stand-By Arrangement, 2004–05 (Concluded)

Measures	Implementation Period	Status of Implementation
<i>Public Enterprises</i>		
Selection of the successful bidder for Gabon Télécom.	End-September 2004	Not met. Delayed to last quarter of 2005.
Achievement of a surplus in 2004 in the operational results of Air Gabon, before depreciation.	End December 2004	Not met.
Preparation by the consultant in charge of the partial privatization of Air Gabon of the documentation to select prequalified bidders. ¹	End-April 2005	Not met. Air Gabon is in process of liquidation.
<i>Trade reform</i>		
Removal of import surcharges on poultry and cigarettes.	End-December 2004	Met.

1/ Structural benchmarks added at the time of the second review of the stand-by arrangement.