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**Republic of Congo: Staff-Monitored Program: Letter of Intent,
Memorandum of Economic and Financial Policies, and Technical
Memorandum of Understanding**

March 27, 2008

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Brazzaville, March 27, 2008

The Minister of Economy,
Finance, and Budget

to:

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
Washington, D.C. 20431
USA

Dear Mr. Strauss-Kahn:

The government of the Republic of Congo (Congo) pursued a Staff Monitored Program (SMP) during April-September 2007, with the intent of establishing a track record of performance that would support a subsequent move to a Poverty Reduction and Growth Facility (PRGF) arrangement. While we made some progress under the SMP, we also had fiscal slippages and did not implement some key structural measures in a timely manner, which prevented the successful completion of this program.

The fiscal slippages were associated mainly with unanticipated costs of the legislative elections last year, higher subsidies to the petroleum sector due to high world oil prices, and higher than budgeted domestically-financed investment. On structural policies, delays in implementation reflected low capacity and the need to enhance program monitoring. In this regard, we established a new reporting and monitoring structure, which will foster strong program ownership and our relations with the IMF. A policy committee headed by the President of the Republic will manage Congo's program and relations with the IMF, and it will be supported by a technical monitoring committee headed by a special advisor to the President of the Republic. The resident representatives of the IMF and the World Bank have been invited to serve as advisors to the technical committee. The technical committee has been heavily engaged with Fund staff, and we believe the flow of information and dialogue has already been improved.

We are determined to make a break from the past, and to establish a satisfactory record of macroeconomic and structural policy implementation. In this regard, we request a new Staff Monitored Program covering the period January 1 through June 30, 2008. The policies and objectives of this SMP are detailed in the attached Memorandum of Economic and Financial

Policies (MEFP). This SMP is designed to facilitate the move to a PRGF arrangement, by demonstrating the government's resolve to pursue fiscal consolidation, enhance governance and transparency, and reassure Congo's external creditors that we are committed to macroeconomic stabilization and structural reform.

We believe that the policies and measures set forth in the MEFP are adequate to achieve the objectives of the program, but we will take any further action that may become appropriate for this purpose. During the implementation of the SMP, we will consult with IMF staff on the adoption of measures that may become appropriate for that purpose, at the initiative of the government, or whenever the IMF staff requests such a consultation.

The government intends to make the contents of this letter, the attached MEFP, and the staff report accompanying this request available to the public, and it authorizes the IMF to post them (after Fund management approval and transmission to the Executive Board) on its external website.

Sincerely yours,

/s/

Pacifique Isoïbeka
Minister of Economy, Finance, and Budget

Attachment: Memorandum of Economic and Financial Policies

ATTACHMENT I**REPUBLIC OF CONGO****Technical Memorandum of Understanding**

January 1 Through June 30, 2008

1. This technical memorandum of understanding (TMU) sets out the modalities for tracking the staff monitored program (SMP) of the government of the Republic of Congo for the period January 1-June 30, 2008.

I. QUANTITATIVE CRITERIA AND INDICATORS

2. **The quantitative indicators are:**

- a. a floor on the basic primary non-oil fiscal balance, cumulative starting from January 1, 2008 for the SMP;
- b. no accumulation of new medium or long term nonconcessional external public or publicly guaranteed debt (including leasing) (a continuous quantitative indicator);
- c. no accumulation of new external public or publicly guaranteed debt (including leasing) with an initial maturity of less than one year (a continuous quantitative indicator);
- d. a ceiling on the accumulation of new oil-collateralized external debt contracted by or on behalf of the central government (a continuous quantitative indicator);
- e. a ceiling on new nonconcessional external debt contracted by the SNPC (with or without government guarantee), starting from January 1, 2008 (a continuous quantitative indicator), unless otherwise indicated in paragraph 12;
- f. no accumulation of new external payment arrears with respect to the service on non-reschedulable external debt (see paragraph 12 below for the definition), starting from January 1, 2008 for the indicators of the first half of 2008 (a continuous quantitative indicator); and
- g. no accumulation of new domestic payment arrears, starting from January 1, 2008 (a continuous quantitative indicator).

II. DEFINITIONS AND COMPUTATION

A. Government

3. Unless otherwise indicated, “government” is defined as the central government of the Republic of Congo and does not therefore include local governments, the central bank, and any public entity with autonomous legal personality not covered by the government’s consolidated financial operations table (tableau des opérations financières de l’Etat—TOFE).

B. Non-Oil Basic Primary Fiscal Balance

4. The scope of the government’s fiscal operations table (TOFE) includes the general budget and the special accounts of the Treasury (including the forestry and road funds) and the government debt management agency (Caisse Congolaise d’Amortissement, CCA).

5. **The government’s non-oil basic primary fiscal balance** is equal to total non-oil revenue excluding grants, minus total expenditure (including net credit), less interest on debt and less foreign-financed public capital expenditure. It is calculated from the budget execution outturn reported every month in the TOFE prepared by the Ministry in charge of finance.

6. **The government’s total revenue is reported in the TOFE on a cash basis.** It includes all revenue collected by the Treasury (including tax and customs receipts, oil revenues, service revenues, and forestry revenues), whether they result from past, current, or future liabilities. Revenues also include those recorded on a gross basis, in the special accounts.

7. **Expenditures are reported on a payment order basis.** They include current expenditures, domestically-financed capital expenditures, foreign financed capital expenditure as well as net lending. Current expenditures include expenditures on wages, goods and services, common charges, interests on debt (domestic and foreign), transfers and subsidies and other current expenditures.

C. Foreign Debt and Arrears

8. **The definition of government used for the various foreign debt indicators** includes government, as defined in paragraph 3, public institutions of an administrative nature, public institutions of a scientific and/or technical nature, public institutions of a professional nature, public institutions of an industrial and/or commercial nature, and local governments, with the sole exception of the national oil company (SNPC)—see paragraph 12 below.

9. For the purposes of this memorandum, “debt” and “concessional loans” are defined as follows:

- As specified in the guidelines adopted by the Executive Board of the IMF,¹ debt will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows: (i) loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements); (ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until some time after the date on which the goods are delivered or services are provided; and (iii) leases, i.e., arrangements under which property is provided which the landlord has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. The debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement, excluding those payments that cover the operation, repair, or maintenance of the property. Under the definition of debt set out above, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.
- Loan concessionality is assessed on the basis of the commercial interest reference rates (CIRRs) established by the OECD. A loan is said to be on concessional terms if, on the date of conclusion of the contract, the ratio of the net present value of the loan, calculated on the basis of the reference interest rates, to its nominal value is less than 50 percent (i.e., a grant element of at least 50 percent). For debts with a maturity exceeding 15 years, the ten-year reference interest rate published by the OECD is used to calculate the grant element. For shorter maturities, the six-month market reference rate is used.

10. The quantitative indicative target related to external debt apply not only to debt as defined in the above-mentioned guidelines, but also to commitments incurred or guaranteed for which no value has yet been received or on which only partial drawings have been

¹ See Executive Board Decision No. 6230-(79/140) as amended by Decisions Nos. 11096-(95/100) and 12274-(00/85).

made. However, this does not apply to financing from the IMF or to Treasury bills and bonds issued by the Congolese Treasury in CFA francs on the CEMAC regional market.

11. For foreign debt with an initial maturity of less than one year, normal short-term import and export credit are excluded from the scope of the indicator, including the prepayments.

12. The ceiling on any new nonconcessional foreign debt with a maturity of more than one year incurred or guaranteed by the SNPC, with or without government guarantee, will be observed continuously. The SNPC may borrow only to finance investments related to its core activities (research, exploration, production, refining and distribution of oil, construction of their Brazzaville headquarters, creation and strengthening of its database, etc.). In addition, these investments must be included in the SNPC's investment budget approved by its board of directors. The ceiling on debt does not apply to changes in loan accounts with oil field partners or to loans with maturities of less than one year.

13. The accumulation by the government of external payment arrears is the difference between (i) the gross amount of external debt service payments due (principal and interest, including moratorium and/or late interest, as appropriate) and (ii) the amount actually paid during the period under consideration. Under the program, the government commits itself to not accumulate external payment arrears on non-reschedulable debt (that is, debt to Paris Club creditors contracted after the cutoff date and debt to multilateral creditors). Non-accumulation of external payment arrears is an indicator to be continuously observed.

D. Oil-Collateralized Foreign Debt

14. Oil-collateralized external debt is external debt which is contracted by giving an interest in oil. Pre-financing is defined as an oil-collateralized loan which is repaid by the sale of the oil in a different calendar year. New pre-financing by or on behalf of the government is strictly prohibited under the program. The refinancing and/or deferral of the existing stock and/or due dates are permitted but should not give rise to an augmentation of the existing stock of oil-collateralized debt. The government undertakes not to contract any new oil-collateralized debt.

III. STRUCTURAL MEASURES

15. Structural measures are listed in Table 2 attached to the Memorandum of Economic and Financial Policies regarding the staff-monitored program:

Structural measures under the SMP

- The government will adopt by March 31, 2008 a comprehensive action plan with a timetable to address institutional and procedural deficiencies in the

commercialization of Congolese oil, to bring them in line with best international practice.

- The government will adopt by March 31, 2008 a comprehensive action plan with a timetable for reforming CORAF, taking on board the recommendations of the diagnostic study of its operations by an international consultant.
- Completion by June 30, 2008 of a technical and financial audit, by an independent, internationally recognized firm, of current transfers and a representative sample of capital expenditures executed during the period from January 1, 2006 to December 31, 2006, based on terms of reference satisfactory to IMF and World Bank staff. Publication of the audit report on the website of the Ministry of Finance (www.mefb-cg.org).
- Adoption by June 30, 2008 of a three-year action plan to strengthen public investment management, with assistance from the French Cooperation agency, World Bank, and other development partners.
- Quarterly adjustment (within four weeks from the end of the quarter) in petroleum entry distribution and/or retail prices to ensure that oil subsidies for 2008 remain within budget limits (CFAF 35 billion for the full year). The price adjustments should not pass-through any decline in world oil prices.
- Quarterly certification, on a continuous basis, of oil revenue by an internationally recognized audit firm—with on quarter lag—using the same specifications as for the 2003 certification and with no restrictions on access to information; certification reports to be published on the website of the Ministry of Economy, Finance, and Budget (www.mefb-cg.org).
- Publication of all invitations to bid and the bids themselves for government procurement contracts above CFAF200 million on the government website (www.mefb-cg.org)
- No granting, on a continuous basis and as of the date of promulgation of the 2008 budget law, of new tax and customs exemptions (except those under international conventions).
- Centralization of all public revenues and execution of all public payments at the Treasury.
- No recourse, on a continuous basis and as of the date of promulgation of the 2008 budget law, to emergency payment and cash advance procedures, except in national situations stated in the organic budget law.

IV. INFORMATION FOR PROGRAM MONITORING

16. The government will submit the following information to the staff of the International Monetary Fund through its Resident Representative, and within the time period specified below.

A. Oil Sector

17. Regarding the oil sector, the government will submit the following information to IMF staff within four weeks after the end of the month:

- the monthly data on oil production by oil field, production costs, volume exported, export prices, and the operations of the national oil company (SNPC);
- the breakdown concerning the share of crude oil that accrues to the government, by oil field, distinguishing the type of resource to which this share relates (royalties, profit oil, etc.);
- any change in the tax parameters; and
- a breakdown of oil prices.

B. Government Finance

18. Regarding government finance, the government will submit the following information to IMF staff:

- A table on government fiscal operations (TOFE) and its annexes. The annexed tables include (i) the breakdown of oil revenue in value terms with the corresponding notes on computation, (ii) excess oil trends and any bonus payments, (iii) the breakdown of tax and nontax revenue, and central government expenditure, particularly transfers and common charges; and (iv) a report on the amounts of and rationales for emergency payment and cash advance procedures. The provisional TOFE and its annexes will be reported monthly within four weeks from the end of the month, whereas the final TOFE and its annexes will be reported within six weeks from the end of each month.
- Monthly data on the prices and taxation of petroleum products. These data will include: (i) the price structure in effect during the month; (ii) the details of computation of the price structure, (f.o.b. Mediterranean price) at retail prices, including the border impact prices, taxes, transit costs, economic adjustments, ex-refinery prices (for CORAF and imports), entry distribution prices, margins and fees, transport costs and losses, financing expenses, and insurance ; (iii) amounts

released for sale; and (iv) a breakdown of the tax revenue from oil products—customs duties and value-added tax—and direct/indirect subsidies incurred by the budget. These data will be reported within four weeks from the end of the month.

- The Treasury balance to monitor expenditures. It will include the amount of commitments, payment orders, and payments, for both current and capital expenditure. It will be produced on a quarterly basis, and submitted to Fund staff no later than four weeks after the end of each quarter.
- Data on implementation of the public investment program, including the breakdown relating to financing sources. If the data on the execution of investments financed with foreign grants and loans are not available on schedule, a linear estimate of execution in comparison with annual forecasts will be used. These data will be reported on a quarterly basis within four weeks from the end of the quarter.
- Complete monthly data on non-bank domestic financing of the budget (net bank credit to, and net non-bank credit to the government). These data will be reported monthly within four weeks from the end of the month.
- The table used to monitor the expenditure process will list the amount of commitments, payment orders, and payments, for both operating and capital expenditures. It will be produced on a quarterly basis, and submitted to Fund staff no later than four weeks after the end of the quarter.
- A quarterly table for monitoring poverty reduction expenditures, based on the pro-poor sectors defined in the interim poverty reduction and strategy paper (I-PRSP)—basic health care and education; infrastructure and rural integration; water and electricity; disarmament, demobilization and reintegration; social protection, and agriculture). The quarterly tables will be submitted within four weeks of the end of the quarter.
- A monthly table of prepayments, which will also indicate the nature of the expenditures (current transfers, investment, etc.) and the justification for the need to use the prepayment option.
- Quarterly financial reports from the main state enterprises, including SNPC, SNE, SNDE, SOTELCO within four weeks of the end of the quarter.
- A provisional income statement of CORAF for 2008 showing the financing requirement from the government. A provisional income statement will be sent to the IMF within four weeks from the end of each quarter.

C. Monetary Sector

19. The government will submit on a monthly basis, within four weeks of the end of the month, the following preliminary information:

- data on net bank credit to the government;
- the consolidated balance sheet of the monetary institutions, the central bank survey, and the commercial banks survey;
- the integrated monetary survey;
- the table of lending and deposit rates; and
- the usual banking supervision indicators for banks and non-bank financial institutions, where necessary.

20. The final data for the integrated monetary survey will be transmitted within six weeks of the end of the month.

D. Balance of Payments

21. The government will submit the following information to IMF staff:

- any revised balance of payments data (including services, private transfers, official transfers, and transactions for the capital and financial account) as soon as the data are revised; and
- foreign trade statistics (volume and price) prepared by the national statistics agency within three months of the end of the reporting month.

E. Debt

22. The government will submit the following to the staff of the IMF within four weeks of the end of the month:

- data on the stock, accumulation, and payment of domestic arrears;
- data on the stock, accumulation, and payment of external payment arrears;
- a breakdown of estimated domestic and external public debt service, service due, and actual payments, including breakdowns of principal and interest and by creditor;

- the list and amounts of new external debt incurred or guaranteed by the government, including detailed information on the terms and conditions (currency, interest rate, grace period, and maturity) stated in the original agreement; and
- actual disbursements of foreign financial assistance (project and non-project), including new borrowing and any external debt relief granted by foreign creditors (CCA tables).

F. Real Sector

23. The government will submit the following to the staff of the IMF:
- monthly itemized consumer price indices, within four weeks of the end of the month;
 - any revision of the national accounts; and
 - any other indicators and statistical data used to track overall economic developments, including information on activity in the forestry sector and wood-processing industry, as well as the short-term economic bulletins prepared monthly.

G. Structural Reforms and Other Data

24. The government will submit the following information to the IMF staff:
- a monthly detailed table concerning the implementation of structural measures under the program;
 - any study or official report on the economy of the Republic of Congo, within two weeks of its publication; and
 - any decision, order, law, decree, ordinance, or circular having economic or financial implications for the program, within two weeks from the time it is published, or, at the latest, from its entry into force.

ATTACHMENT II

Memorandum of Economic and Financial Policies

January 1 Through June 30, 2008

I. BACKGROUND

1. Under Congo's Poverty Reduction and Growth Facility (PRGF) arrangement approved by the Fund's Executive Board in December 2004, the government implemented a number of reforms aimed at stabilizing the macroeconomic situation, enhancing transparency, governance, and public financial management. Together with favorable external developments and internal peace and social stability, the successful implementation of the PRGF arrangement during 2004-06 allowed Congo to achieve a number of important objectives:

- Overall real GDP growth was relatively strong during this period, averaging about 6 percent and this included an expansion of the non oil sector of a slightly lower magnitude. Inflation averaged about 3 percent per year, broadly in line with the CEMAC convergence criterion.
- The external position strengthened markedly, reflecting increasing oil production and favorable world oil prices. At the end of 2006, our foreign reserves increased to the equivalent of 10½ months of imports (about US\$ 1.8 billion) from only 1.4 months at end-2004.
- The decision point under the enhanced Heavily Indebted Poor Countries (HIPC) Initiative was reached in March 2006, and we benefited from a debt rescheduling from the Paris Club, and interim relief under the enhanced HIPC Initiative from some multilateral and bilateral creditors.

2. Regrettably, we could not conclude the third review under the PRGF arrangement in 2006 because of fiscal slippages and delays in structural reform.. To signal our intention to resume support under the PRGF we requested a Staff Monitored Program (SMP) covering the period April through September 2007, but persistent fiscal slippages, weaknesses in institutional and administrative capacity, as well as unforeseen factors, compromised the implementation of the program.

3. We recognize that weak program ownership has played an important role in unsuccessful policy implementation. For this reason, we have established a new reporting and monitoring structure, which we believe will result in strong performance under this

new SMP, and later under a PRGF arrangement. A policy committee headed by the President of the Republic will manage Congo's programs and relations with the Fund and World Bank, and it will be supported by a technical monitoring committee, headed by a special advisor to the President of the Republic. The resident representatives of the IMF and the World Bank have been invited to serve as advisors to the technical committee. For the Fund's part, we are encouraged by the efforts to streamline conditionality and ensure its macro relevance. We believe that, together, these developments will improve the likelihood of program success, which is critical to Congo's key objectives of enhancing growth, reducing poverty, and achieving external sustainability through debt relief under the enhanced HIPC Initiative.

II. RECENT DEVELOPMENTS

4. Overall economic activity declined in 2007 because of a temporary fall in oil production caused by an accident on the Nkossa oil platform. However, the non oil economy continued to expand at a healthy pace (about 6½ percent), and above the growth rate experienced during the past several years. Food prices fell as a result of improvements in the transportation network, leading to a decline in annual inflation in 2007. The current account moved into deficit last year, reflecting the decline in oil production and imported equipment to repair the oil platform. The external position, however, was helped by an agreement with London Club creditors, which led to debt relief amounting to US\$ 1.6 billion. This agreement is consistent with the enhanced HIPC Initiative and accounts for more than half of the total relief envisaged at the completion point.

5. Monetary conditions were appropriate for Congo during 2007. Broad money slowed from its strong increases in previous years, which reflected the build up of government deposits with commercial banks. The financial sector remained sound according to the regional banking supervisor (COBAC). A new bank specializing in home mortgages was recently created and a new commercial bank has just been licensed.

6. The fiscal stance weakened in 2007 because of an overshoot in expenditure. The overshoot was associated mainly with unanticipated costs of the legislative elections last year (some re-voting took place because of irregularities in some constituencies), higher subsidies to the petroleum product sector due to high world oil prices, and higher than budgeted domestically-financed investment. In the latter case, we had intended to limit this investment to CFAF 344 billion, but it proved difficult to reverse the over execution of this spending which took place in the third quarter of the year. Overall, these developments, together with a decline in oil revenue (related to the temporary decline in oil production), resulted in a sharp fall in the basic primary surplus to about 13.9 percent of GDP in 2007, from 21.5 percent a year earlier.

7. While there were delays in implementing structural reform under the previous SMP, important progress has been made more recently. We completed several audits that were undertaken to help increase the transparency of oil costs and revenue. We took actions to enhance governance through the creation of an anti-corruption observatory, sending them the audit report on the award of Marine XI concession. We presented a draft law to parliament on conflict of interest and asset disclosure of public officials, and adopted a decree to ensure that all new oil concessions will be awarded through a competitive bidding process. We re-entered the Kimberly process for diamond certification and re-applied to the Extractive Industries Transparency Initiative (EITI). We completed diagnostic studies on how to improve the financial and operating performance of the national oil refinery and the oil-marketing company (SNPC). As agreed with Fund staff, the government raised petroleum product prices earlier this year, to help reduce subsidies to the petroleum product sector, which had been a major source of fiscal slippage last year. Finally, we have adopted a public finance reform program with the support of the Fund, World Bank, European Union, and other donors.

III. MEDIUM-TERM OBJECTIVES AND POLICY FRAMEWORK

8. The Poverty Reduction Strategy (PRS), which is expected to be finalized shortly, provides the foundations for the government's medium-term policy framework. This framework is based on the need to: (i) diversify the economy to reduce our dependence on oil, which we recognize fully as an exhaustible resource; (ii) enhance public financial management and the management of our natural resources (including oil, forests, and minerals); (iii) build human capital, by improving the allocation of resources in the social sector (health and education); (iv) continue to improve governance and transparency, which would bolster Congo's attractiveness for domestic and foreign investment; (v) rebuild the country's economic infrastructure, especially the transportation network; (vi) and consolidate macroeconomic stability. We believe that we have the financial resources necessary to achieve these broad objectives, but we also require technical assistance to increase institutional and administrative capacity. Here, strong donor coordination could help buttress our own efforts.

9. In the event, economic policies over the medium term will be aimed at:

- Overall real GDP growth of 9-10 percent through 2010 and continued robust activity in the non oil economy. This would yield good progress toward reaching the income Millennium Development Goal.
- Inflation of about 3 percent per year, which is in line with the CEMAC convergence criterion, which would help preserve Congo's international competitiveness under the fixed exchange rate regime.

- Gradual but continued fiscal consolidation to ensure that the nation's oil wealth is preserved over the long term, and to improve the contribution of the non oil sector to national wealth. By doing so, this will help prevent a decline in living standards when oil production declines. In this regard, we will target a progressive decline in the non-oil primary deficit over the medium term. Achieving this objective will require tight control over current and capital spending, which will be supported by concerted effort to enhance public financial management.
- External sustainability, through prudent debt management and benefiting from HIPC debt relief.

IV. ECONOMIC POLICIES FOR 2008 UNDER THE SMP

10. The economic outlook for 2008 appears favorable, with continuing high world oil prices, an increase in oil production, and a buoyant non oil sector driven by strong domestic demand. Overall real GDP growth is projected to be about 9 percent, with low inflation. Oil receipts are expected to boost official reserves to a record 19 months of imports (39 percent of GDP), which further strengthens our external position and provides a buffer against exogenous shocks. To achieve these objectives, the fiscal stance will be tightened and the regional central bank will contain the growth of broad money. Structural policies will focus on improving public financial management and the financial and operating performance of key state-owned enterprises in the oil sector, and complete the reform agenda from last year.

A. Fiscal Policy

11. The key fiscal objective is to reestablish the credibility and integrity of the budget as the government's main fiscal instrument. This implies keeping within the budgeted envelope for all categories of expenditure, including capital, eliminating the recourse to emergency and cash advance payment procedures, and ensure the timely receipt of oil revenue in conformity with the organic budget law.

12. Parliament has endorsed the 2008 budget, which is broadly in line with understandings reached with Fund staff. The program targets a domestic basic primary surplus of about 22 percent of GDP, which is a dramatic improvement over last year. This is equivalent to a reduction in the non oil primary deficit of about 15 percentage points of non oil GDP, to about 41 percent of non oil GDP.

13. The improvement in the primary surplus reflects a rolling back of previous fiscal slippages, as total revenue remains broadly the same as last year (at about 20 percent of non-oil GDP). We have not introduced new taxes in the budget, but we will protect the revenue target through a number of ongoing measures. These include: the regular and

timely transfer of (certified) oil receipts to the budget; the centralization of all public revenue; tax and customs administration reform through computerization and implementation of recent recommendations from audits in these areas; fight against fraud and tax evasion; and the progressive reduction of, and, no granting of new tax and customs exemptions (except those in international conventions, structural benchmark).

14. On primary spending, the 2008 budget envelope has been reduced by about 15 percentage points of non-oil GDP to about 61 percent of non-oil GDP. We will achieve the reduction in annual spending mainly through an expected decline in litigation fees related to our external liabilities, lower subsidies to the petroleum product sector because of the increase in petroleum prices, and through a stabilization of domestically-financed capital spending. Despite our strong desire for increasing capital spending—given our pressing infrastructure needs—the level of capital spending will be reduced by CFAF 28 billion compared to the budget, in order to take into account the acceleration of some disbursements in the latter part of last year, capacity considerations, and the need to assess the effectiveness of our investment program before ratcheting it up further. An audit of a sample of such spending associated with 2006 and current transfers, will be completed by end-June 2008 (structural benchmark), and, together with World Bank assistance with developing an action plan by end-June 2008 to improve public investment management (including aligning it with the PRS) (structural benchmark), we could anticipate expanding our capital budget in the medium term. Oil subsidies have weighed heavily on the budget in the past and to alleviate this burden, we will, if necessary, undertake quarterly adjustments in petroleum entry distribution and/or retail prices to stay within the budgeted ceiling (structural benchmark). The need for, and size of, domestic fuel price adjustments will largely be determined on the basis of CORAF's financial position through the year. The 2008 budget provides for an increase in pro-poor spending and a CFAF 20 billion (about 1.3 percent of non-oil GDP) contingency reserve, which we have set aside to help avoid further fiscal slippages.

15. We have established an action plan aimed at improving public financial management (with assistance from the Fund, World Bank, and other donors), which is a prerequisite for expanding the budget envelope further. As part of this action plan, we intend: to adopt the presidential decree establishing the new functional budget classification system (by-end March 2008), and use it for implementation monitoring; continue to apply a monthly monitoring system to ensure that cash advance and exceptional payment procedures are not used, in line with the organic budget law (structural benchmark); improve the expenditure chain from commitment to execution; make progress in establishing a new procurement code; and establish an adequate management and control framework, for the use of HIPC resources. Once these requirements are met, the government intends to use these HIPC resources in line with understandings reached earlier with our development partners. Also, to strengthen control over public spending, the

Ministry of Finance and Budget will provide training and hold seminars to build capacity of budget managers in line ministries, and immediately issue a Ministerial order which will prohibit payment orders beyond the budgeted amounts across all ministries, departments, and agencies.

16. In the same vein, we will continue to pursue the implementation of measures aimed at improving the governance, transparency, and the management of natural resources. These measures include: the quarterly certification of oil revenue by an internationally recognized audit firm (structural benchmark); the audit of oil costs for productions sharing agreements; and awarding of new oil concession contracts through a competitive bidding process. Also, we will make a determined effort to implement the requirements of the EITI.

B. Monetary and Financial Sector Policies

17. Monetary and exchange rate policy is conducted at the regional level by the Bank of Central African States (BEAC) and Congo is a member of the CEMAC region whose common exchange rate is fixed to the euro. During the next year or so, the BEAC will continue to focus on achieving low inflation and reserve accumulation in support of the exchange rate peg. At the national level, to enhance liquidity management and separate monetary from fiscal policy, we will (i) make efforts to repay accumulated statutory advances (amounting to CFAF 154 billion), given the high cost of holding these advances (interest rates are above 5 percent) and the government's significant cash position and BEAC deposits, and (ii) progressively move towards a single Treasury account at the central bank, as recommended by the report on the regional Financial Sector Stability Assessment completed in 2006.

18. We have recently completed (with Fund and World Bank assistance) an action plan for the development of the financial sector. With our CEMAC partners, we envisage taking a number of actions in the near term that should help expand private sector credit, including the liberalization of lending and deposit rates, and to finalize the corporate financial statement registry, the central credit bureau, and the payment risk management system. These reforms should increase information available to borrowers and investors as well as decrease the cost of borrowing for smaller enterprises. The audit of the two pension Funds; the National Social Security (*Caisse nationale de sécurité sociale*) and the Government Employee Pension (*Caisse de retraite des fonctionnaires*) were completed recently. These audits include recommendations to place these Funds on a sound financial footing, while updating the regulatory and supervisory framework. In the area of Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT), we will continue our efforts to establish by end-March 2008 the National Financial Investigation Unit (*Agence Nationale d'Investigation Financière*, ANIF), in compliance with CEMAC regulations. Other measures that we intend to implement at the national level over the

medium term include actions aimed at improving the business environment and legal and accounting frameworks.

C. External Debt Management

19. The government is in the process of formulating a new external debt management strategy, although there is no intention of seeking foreign loans on non-concessional terms. Rather, this strategy is being designed to help strengthen debt management procedures and criteria, as well as institutional capacity to contract and monitor the debt by public sector entities, and minimize the risk of default. To diversify the sources of financing, the new strategy will introduce a domestic debt issuance policy, in line with the regional CEMAC guidelines. While debt management will remain the responsibility of the Ministry of Finance, a new National Debt Committee will provide support to the new debt strategy. We will continue centralizing debt data at the debt management unit (Caisse Congolaise d'Amortissement), including collateralized debt, and publishing the related data and projections on the government external site during the first half of this year. Also, we will ensure consistency of our data, reconcile them regularly with the balance of payments and budget, and publish an annual national debt report.

20. The government will step up efforts to normalize relations with external creditors. Following the recent agreement with the London Club, we are seeking comparable treatment from suppliers, non-London Club commercial creditors, and litigating creditors. The government will also seek to sign bilateral agreements with the remaining Paris Club creditors as soon as possible.

V. Reform of State-Owned Enterprises

21. Improving the operating and financial performance of the national oil refinery (CORAF) and more effective commercialization of government oil (through SNPC) are important aspects of the governance agenda. Over the medium term, the government intends to develop a comprehensive strategy aimed at improving sector performance through upgrading SNPC's accounting framework, monitoring closely the technical and economic aspects of the operations of private oil companies, developing a sector data base, and evaluating all possible institutional, contractual, and regulatory reforms that could ensure that Congo is obtaining the maximum benefit—while respecting its legal obligations and the sanctity of private property rights—from its oil resources. To undertake some of this work, the government intends to prepare terms of reference (by mid-year) and obtain adequate sector expertise, including from the World Bank.

22. By end-March 2008, the government will adopt a comprehensive action plan with a timetable for reforming CORAF (structural benchmark), taking on board the

recommendations of the diagnostic study of its operations by an international auditor completed earlier. Among other things, this plan should include measures: to address priorities for rehabilitation investment and the operational improvements suggested by the auditor; allow CORAF to become an independent cost and profit entity, establishing its own analytical accounting system, and able to purchase the adequate crude oil and to independently export surplus products, and to move out of the refinery accounts the petroleum products remaining subsidies by establishing a pricing system with export-import price parities. For the SNPC, the government will adopt a comprehensive action plan with a timetable by end-March 2008 (structural benchmark) to address institutional and procedural deficiencies in the commercialization of Congolese oil, to bring them in line with best international practice. As part of their efforts to enhance transparency, the authorities will continue with the practice of conducting and publishing audits of oil costs in the years ahead.

VI. PROGRAM MONITORING UNDER THE SMP

23. The SMP will be monitored through staff assessments based on quantitative targets and structural benchmarks for end-March and end-June 2008, as set out Tables 1 and 2, respectively. Detailed definitions and reporting requirements for all quantitative indicators and structural benchmarks are contained in the accompanying Technical Memorandum of Understanding (TMU, Annex II). The authorities will make available to Fund staff all core data, appropriately reconciled, and on a regular and timely basis, as specified in the TMU.

24. The first staff assessment of the SMP is expected to take place in May 2008, with the second review in August, if the relevant data and information is made available.

Table 1. Republic of Congo: Proposed Quantitative Indicative Targets, Jan 1 - Jun 30, 2008
(Billions of CFA francs, unless otherwise indicated; cumulative from January)¹

	End-Mar. 08	End-Jun. 08	End-Sep. 08	End-Dec. 08
	Target	Target	Indicative Target	Indicative Target
Quantitative targets				
Nonoil primary fiscal balance (floor)	-198.5	-387.1	-506.8	-629.2
New medium or long-term nonconcessional external debt (including leasing) contracted or guaranteed by the government (ceiling) ^{2, 3}	0.0	0.0	0.0	0.0
New external debt (including leasing) with an original maturity of less than one year (ceiling)	0.0	0.0	0.0	0.0
New oil-collateralized external debt contracted by or on behalf of the central government (ceiling) ³	0.0	0.0	0.0	0.0
New nonconcessional external debt contracted by SNPC (ceiling) ³	0.0	0.0	0.0	0.0
New external arrears on nonreschedulable debt ³	0.0	0.0	0.0	0.0
New domestic arrears ³	0.0	0.0	0.0	0.0
Memorandum items				
Oil revenue (in billions of CFA francs)	338.5	709.1	1130.9	1571.1
Non-oil revenue	77.0	153.9	230.9	307.8

¹ Quantitative indicative targets are defined in the attached technical memorandum of understanding.

² Excluding rescheduling arrangements and disbursements from the IMF; the minimum grant element is set to 50 percent.

³ Continuous.

Table 2. Structural Benchmarks Under the SMP, January 1–June 30, 2008

Measures	Date
The government will adopt a comprehensive action plan with a timetable to address institutional and procedural deficiencies in the commercialization of Congolese oil, to bring them in line with best international practice.	March 31, 2008
The government will adopt a comprehensive action plan with a timetable for reforming CORAF, taking on board the recommendations of the diagnostic study of its operations by an international consultant.	March 31, 2008
Completion of a technical and financial audit, by an independent, internationally recognized firm, of current transfers and a representative sample of capital expenditures executed during the period from January 1, 2006 to December 31, 2006, based on terms of reference satisfactory to IMF and World Bank staff. Publication of the audit report on the website of the Ministry of Economy, Finance, and Budget (www.mefb-cg.org).	June 30, 2008
Adoption of a three-year action plan to strengthen public investment management, with assistance from the French Cooperation agency, World Bank, and other development partners.	June 30, 2008
Quarterly adjustment in petroleum entry distribution and/or retail prices to ensure that oil subsidies for 2008 remain within budget limits (CFAF 35 billion for the full year). The price adjustments should not pass-through any decline in world oil prices.	Four weeks after the end of each quarter
Quarterly certification of oil revenue by an internationally recognized audit firm, using the same specifications as for the 2003 certification and with no restrictions on access to information; certification reports to be published on the website of the Ministry of Economy, Finance, and Budget (www.mefb-cg.org).	Continuous, with a one-quarter lag
Publication of all invitations to bid and the bids themselves for government procurement contracts above CFAF200 million on the government's website (www.mefb-cg.org).	Continuous
No granting of new tax and customs exemptions (except those under international conventions).	Continuous
Centralization of all public revenues and execution of all public payments by the Treasury.	Continuous
No recourse to emergency payment and cash advance procedures, except in situations stated in the organic budget law.	Continuous