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Cameroon: Letter of Intent

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LETTER OF INTENT

June 18 , 2009

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

Dear Mr. Strauss-Kahn:

1. The conclusions of the Article IV consultation mission to Cameroon indicated that our country's economic situation, which had improved significantly with the implementation of reforms supported by the most recent PRGF arrangement (October 2005–January 2009), will deteriorate owing to the international economic crisis.

2. The Cameroonian economy remains vulnerable to fluctuations in global demand and commodity prices. In particular, the sharp decline in oil revenues this year will lead to a deterioration in the fiscal and external balances. These tighter financial conditions will make the government's efforts to accelerate economic growth, particularly through public investment, more challenging. Despite the progress made to consolidate macroeconomic stability, poor infrastructure and an unfavorable business environment still hamper economic activity and make it difficult to reach the growth rates needed to reduce poverty on a sustainable basis.

Impact of the Shocks

3. The global slowdown is having a severe impact on the Cameroonian economy through several channels:

- Lower international oil prices, which will lead to a significant deterioration in the terms of trade, as well as a substantial drop in fiscal oil revenues;
- Weaker external demand for our main export products, particularly timber, cotton, rubber, and aluminum;
- Tighter international financial conditions, which could delay some of our large mining and infrastructure projects;
- Reduced transfers from Cameroonians working abroad.

4. This situation will negatively affect our net external balance and our economic growth, which could decline from 3½ percent in 2008 to 2½ percent in 2009. The overall fiscal balance could also turn into a deficit of about 1 percent of GDP in 2009, while the balance of payments deficit could stand at around 4½ percent of GDP. The government is concerned by the magnitude of this deterioration (several percentage points of GDP).

Policies to Address the Shocks

5. To deal with this situation, the government has taken the immediate decision to maintain the priority expenditures included in the 2009 budget. It intends to use the available fiscal space to protect the economy from the effects of the global crisis and continue to lift the infrastructure bottlenecks hampering economic development. The government has also reaffirmed its commitment to eliminating subsidies on fuel prices and resuming implementation of the mechanism for adjusting the retail prices of petroleum products. To protect the most vulnerable segments of the population, it will continue its efforts to strengthen the social safety net, and look at the modalities and mechanisms for introducing a more targeted system.

6. The government has also taken measures to provide assistance to sectors in distress, particularly with a view to help small producers. In the timber sector, it has eliminated the bank guarantee required from taxpayers at the beginning of each fiscal year. It has also eliminated the factory admission tax for products entering second and third processing, thus reducing the cascading tax distortions adversely affecting the sector. It is also planning to reduce the annual timber royalty by half this year to take into account the decline in demand and lower prices for forestry products. In the cotton sector, the outstanding VAT credits have been cleared. Given the tight financial situation for small producers, there is a risk that many of them will lose their source of revenue this year if they are not able to produce. In this regard, discussions are ongoing with operators in the agricultural sector on the possibility of subsidizing inputs.

7. In this context, the government is committed to contain the overall fiscal deficit in 2009 to about 1 percent of GDP and the nonoil primary deficit to about 4 percent of GDP. For this purpose, it will adopt a supplementary budget in 2009 to reflect the decline in oil and nonoil revenues. On the expenditure side, the supplementary budget will take account of the need to maintain the initially planned priority expenditures, support the sectors in crisis, and eliminate arrears in the payments to SONARA to cover its losses incurred in 2008 as the result of the government's policy on retail prices for petroleum products.

8. The government also undertakes to respond to the exogenous shocks by implementing economic policies aimed at reducing the vulnerability of the Cameroonian economy while maintaining macroeconomic stability. To that end, it will take steps to: (i) increase nonoil revenues; (ii) diversify the sources of public financing; (iii) strengthen public expenditure management; (iv) improve the business environment; and (v) preserve the

stability of the financial sector. In addition, the government will avoid introducing or intensifying trade restrictions.

Increasing nonoil revenues

9. The government will step up its efforts to mobilize nonoil revenues by expanding the tax base. To that end, the following measures will be implemented:

In regard to internal revenue:

In 2009

- Simplify tax payment and filing procedures by cutting the number of forms to be filed by half, and hence reducing the high cost of tax compliance;
- Bring back into the general tax regime 19 enterprises identified as still benefiting unduly from exemptions;
- Establish management centers (offering tax and accounting services to small and medium-sized enterprises) to encourage operators in the informal sector to register with the tax administration, and improve and simplify the tax returns of operators already registered;
- Finalize the computer connection between the Ministry of Finance and the Ministry of Forestry and Wildlife to improve the exchange of information on taxpayers.

In 2010

- Complete the work to update the fiscal cadastre in order to expand the property tax base;
- Implement electronic filing to continue to reduce the cost of tax compliance.

In regard to customs revenue:

In 2009

- Improve the use of ASYCUDA (computerized customs system) through better tracking of its risk indicators to combat customs fraud;
- Introduce and use a GPS-based tracking mechanism to improve the monitoring of merchandise in transit and combat fraud affecting customs revenues;
- Accelerate implementation of the import duty sticker for tobacco and alcohol to combat smuggling and increase customs revenues.

In 2010

- Install ASYCUDA at other major revenue-collection posts, in particular Maroua and Garoua-Boulai, and establish computer connections between existing posts where ASYCUDA is installed;
- Computerize procedures and enhance data sharing by improving the electronic one-stop shop;
- Introduce a value registry to ensure proper application of the transaction value and achieve a better assessment of declared values.

Diversification of the sources of public financing

10. To diversify the sources of financing for the economy, the government plans to issue bonds in the coming year, as soon as the subregional mechanism is operational.

Improvement of public expenditure management

11. The government will continue its efforts to improve the quality of public spending to better match committed expenditures to services provided, and achieve savings that can be reallocated to priority outlays. To that end, starting in 2009 it will undertake a quarterly revision of the reference prices for government orders to limit overcharging and ensure the effectiveness of public spending.

12. Increasing public investment will be an essential component of our policy to foster economic recovery. The government undertakes to continue to: (i) improve the tracking of government spending; and (ii) strengthen capacity to prepare, evaluate, and implement projects. To that end, a consulting unit with government participation will be created in 2010 to build capacities for evaluating projects and ensuring that projects included in the government budget are carried through to completion.

13. The government will also take measures to improve fiscal transparency. The government intends to continue to publish quarterly reports on budget execution. The presentation of government financial operations (TOFE) on a payment order basis will be finalized in 2009 and will thereafter be produced on a regular basis to give a more complete picture of the government's fiscal commitments. In addition, the government recognizes the need to avoid excessive accumulation of arrears and treasury float. To that end, it will settle amounts remaining due to SONARA in 2009 and will continue its efforts to strengthen expenditure management.

14. A number of steps currently under way for the gradual implementation of the new public finance system law will be completed in 2009, in particular: (i) the drafting of the decree regulating government accounting, clarifying the fiscal operations of the government,

the parties concerned, and their respective roles in the new environment; and (ii) the drafting of the methodological guide on the preparation of program budgets.

Improvement of the business environment

15. The authorities will give priority to development of the private sector in order to expand and diversify the production base and thus help to reduce the vulnerability of the economy to exogenous shocks. Emphasis will be placed on improving the business environment and combating corruption. To that end, the government is taking steps to create a more favorable environment for foreign investment with the help of the IFC. In 2009, planned priority actions focus on the simplification of procedures for establishing companies and improvement of cross-border trade.

Protection of the stability of the financial sector

16. Although contagion from the international financial crisis via financial channels seems very unlikely in Cameroon, a lasting slowdown in economic activity could increase the vulnerability of banks. To that end, the government will continue to work with the relevant regional authorities to strengthen surveillance of the banking system and limit any potential cost for the budget, while ensuring in particular that banks provision appropriately against nonperforming loans and that the needed corrective measures are taken.

Request for Fund Assistance under the Rapid-Access Component of the ESF

17. Despite these measures, the effects of the international crisis will result in an increased need for budget financing. In the absence of an operational government bond market, the overall fiscal deficit expected in 2009 could be financed by drawing on government deposits at the BEAC.

18. However, the current level of these deposits is appropriate to provide some guarantee in the face of: (i) uncertainties regarding the length of the international crisis; (ii) oil price volatility; (iii) the vulnerabilities of the banking sector; and (iv) the lack of a government bond market. To protect priority spending and not jeopardize poverty reduction efforts, it will be necessary to access other sources of financing.

19. Given the scope of these financing needs, the government has initiated discussions with its development partners to seek their assistance. Moreover, it is anticipated that the new Poverty Reduction Strategy Paper (PRSP) will be completed in August 2009 at the latest. This will be an important milestone for our dialogue with our partners and will lay the foundation for discussions with the IMF on a new program supported by the PRGF by end-2009.

20. However, the mobilization of this financing will take time. We request, therefore, that the IMF allow the government of Cameroon the maximum access of 50 percent of quota (SDR 92.85 million) through the rapid-access component of the Exogenous Shocks Facility (ESF).

21. The government of Cameroon authorizes the IMF to publish this letter.

Sincerely yours,

/s/

Inoni Ephraim
Prime Minister and
Head of Government