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

December 4, 2009

The following item is a Letter of Intent of the government of Senegal, which describes the policies that Senegal intends to implement in the context of its request for financial support from the IMF. The document, which is the property of Senegal, is being made available on the IMF website by agreement with the member as a service to users of the IMF website.
LETTER OF INTENT

Dakar, Senegal
December 4, 2009

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

Dear Mr. Strauss-Kahn:

1. The attached Memorandum of Economic and Financial Policies (MEFP) reviews recent economic developments and implementation of the government of Senegal’s macroeconomic and structural program under the country’s three-year Policy Support Instrument (PSI), approved by the IMF Executive Board on November 2, 2007, and the Exogenous Shocks Facility (ESF) arrangement, approved on December 19, 2008, and augmented and extended on June 19, 2009. The attached MEFP builds on previous Memoranda, and sets out policies the government intends to implement with emphasis on measures and objectives for 2010.

2. All quantitative assessment (performance) criteria for June 2009 and all quantitative indicative targets for September 2009 were met. Structural reforms, which are focused on public financial management, have generally progressed in line with the program despite some delays. Given the complexity of the task, the government is in the process of finalizing the procedures regarding regularization of extrabudgetary commitments and the debt of public agencies and institutions, and has therefore not been able to incorporate them in the 2010 budget law. The government will submit to parliament by May 15, 2010, a supplementary budget containing the specific entries and budget lines to settle these payments. As described in the attached MEFP, the government continues to pursue an ambitious program of budget and fiscal reform, governance reform, and energy sector reform.

3. To supplement resources from donors and the private sector, the government is mobilizing external funds for the Dakar-Diamniadio toll highway. To this end, the government requests to raise the ceiling for non-concessional borrowing for this project by CFAF 10 billion (less than 0.2 percent of GDP) to CFAF 90 billion. The higher ceiling would allow the government to accommodate possibly higher costs and issue a bond in international markets of $200 million, typically seen as a minimum size for this type of transaction. The small increase would have no negative impact on debt sustainability.
4. In light of our overall performance and based on the policies set forth in the attached MEFP, we request completion of the fourth review of the PSI and the second review of the ESF arrangement with a disbursement in the amount of SDR 32.36 million.

5. The government believes that the policies and measures set forth in the attached MEFP are sufficiently strong to achieve the objectives of the PSI-supported program and ESF arrangement. It will promptly take any additional measures necessary for the achievement of the objectives of the program. The government will consult with the IMF—at its own initiative or whenever the Managing Director of the IMF requests such a consultation—before the adoption of any such measures or changes to the policies described in the attached Memorandum. The government will provide the IMF with such information as the IMF may request in connection with the progress made in implementing the economic and financial policies and achieving the objectives of the program. It is expected that the fifth review of the PSI and third review of the ESF will be completed by May 28, 2010.

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

Sincerely yours,

/s/
Abdoulaye Diop
Minister of State
Minister of Economy and Finance

Attachments:  - Memorandum on Economic and Financial Policies (MEFP)
              - Technical Memorandum of Understanding (TMU)
MEMORANDUM ON ECONOMIC AND FINANCIAL POLICIES

Dakar, December 4, 2009

I. INTRODUCTION

1. This memorandum updates Senegal’s economic program under the three-year Policy Support Instrument with the IMF for the period 2007–10 and the Exogenous Shocks Facility arrangement since December 2008. The program supported under the PSI focuses on (i) pursuing a prudent fiscal policy and preventing a recurrence of payment delays; (ii) strengthening governance and transparency; (iii) promoting private sector activity; and (iv) enhancing the contribution of the financial sector to the economy. This memorandum describes recent economic developments and program implementation followed by a discussion of the economic outlook for 2010 and the government’s commitments to pursuing macroeconomic and structural reforms.

2. In a challenging external environment, the government remains committed to preserving macroeconomic stability, fostering good public financial management, strengthening growth driven by the private sector, and making rapid progress toward achieving the Millennium Development Goals (MDGs). The government has demonstrated a determined approach to overcoming its budget execution problems. The extent of these problems was defined in mid-2008 thanks in particular to program measures. Decisive improvements were made in correcting payment delays to the private sector and implementing ambitious reforms to improve the efficiency and transparency of public financial management. Continued progress in this area, in particular settling extrabudgetary commitments and agency debts, should make it possible to fully normalize relations with the private sector. This will also allow the government to broaden the focus of its reforms.

II. RECENT ECONOMIC DEVELOPMENTS, SHORT-TERM OUTLOOK, AND PROGRAM PERFORMANCE

3. Macroeconomic performance in 2009 was modest. The global financial crisis had a marked impact on Senegal’s economy but domestic factors also played a role.

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1 Details of this program were set out in the initial MEFP of October 3, 2007 and in the MEFPs of May 30, 2008, December 5, 2008, and June 5, 2009.
• Real GDP growth slowed. During the first three quarters of 2009, business activity remained weak. The general activity index (excluding agriculture and administration) was flat (year-on-year). Recent flooding and electricity outages exacerbated economic challenges. Growth is expected to be around 1.2 percent in 2009. Relatively robust performance of the primary sector is due to favorable weather as well as an active agricultural policy. In the secondary sector, Industries Chimiques du Sénégal (ICS) pursued its recovery efforts but was faced with much reduced output prices. The tertiary sector, a traditional driving force of the Senegalese economy, registered unsatisfactory results.

• Consumer price inflation (year-on-year) turned negative in May, largely because food and energy prices fell.

• The external current account deficit is projected to improve compared to 2008, primarily as a result of the decline in oil and food prices for the year as a whole.

4. **All quantitative program criteria for end-June 2009 and quantitative indicative targets for end-September 2009 were met.**

(a) The basic fiscal balance ceiling for June 2009 was observed despite a decline in revenues as compressed capital spending and reduced current spending more than offset the revenue loss. As planned, the government eliminated the butane gas subsidy at end-June 2009. The basic fiscal deficit at end-June 2009 amounted to CFAF 19.2 billion, compared to a program ceiling of CFAF 60 billion. Preliminary data indicate that the basic fiscal balance ceiling for end-September 2009 (indicative target) was also observed.

(b) At end-June 2009 the budgetary float had declined to a normal level of CFAF 41 billion (¾ percent of GDP) from CFAF 175 billion (3 percent of GDP) in October 2008. At end-September 2009, the budgetary float amounted to CFAF 42 billion, also below the ceiling of CFAF 45 billion.

(c) The government did not accumulate any external payment arrears.

(d) It has not contracted or guaranteed any nonconcessional borrowing since the second PSI program review, including the CFAF 80 billion for the autoroute (toll highway) permitted under the program.

(e) It has not approved any Treasury cash advances since end-2008 and has executed budget expenditure according to the normal and simplified procedures.
The government limited single-tender contracts to 14 percent of all government procurement in the second quarter of 2009 and 5 percent in the third quarter of 2009 (compared to a program ceiling of 20 percent).

5. Significant progress was also made regarding structural reforms. The majority of structural benchmarks were met and the government is in the process of addressing previous delays.

(a) Following the audit by the Financial Audit Inspectorate (IGF), an independent external audit for extrabudgetary expenditure was completed in July 2009. It identified extrabudgetary spending of CFAF 37 billion and public agency and institution debt of CFAF 67 billion as of December 31, 2008. The government made an initial assessment regarding the claims that are to be settled (structural benchmark, end-July 2009).

(b) The first audit reports of the procurement regulatory agency (ARMP) have been completed. These reports enhance budget transparency and governance and assist in assessing the operation of the new government procurement framework.

(c) The government has prepared a report on the current level of tax expenditures (structural benchmark, end-September 2009). The report highlights key tax expenditures. The analysis suggests that tax exemptions and other forms of tax expenditures could be equivalent to 3¾ percent of GDP.

(d) A completed external audit of the IT infrastructure of the expenditure tracking system, SIGFIP, and an expert review of the system (supported by the IMF’s Fiscal Affairs Department) have provided a sound basis for strengthening budget monitoring (structural benchmark, end-September 2009).

(e) For the 2010 budget newly agreed procedures are being followed. The presentation of the proposed budget has been improved to make it more flexible and information more understandable and transparent by moving towards international best practices (structural benchmark, October 15, 2009). The budget contains (i) a contingency expenditure line of 5 percent of current expenditure excluding personnel outlays; (ii) an annex with execution and forecast data for each agency, para-public sector enterprise, and other public entity receiving budgetary allocations of more than CFAF 5 billion; and (iii) SIGFIP data on budget execution for the past year and the first six months of the current year. Some aspects could be improved further. Specifically, the budget should (i) contain budget execution data for the past year and the first six months of the current year using TOFE data; and (ii) also provide a contingency expenditure line of five percent of capital expenditure, excluding externally funded expenditure. The government will include this information in future budgets.
The government made progress with the use of SIGFIP and ASTER as complementary information systems to improve the preparation, execution, and monitoring of fiscal and accounting operations and make the production of the financial operations table (TOFE) more reliable. The ASTER auxiliary expenditure module will be operational with a delay (structural benchmark end-October 2009). The general expenditure accounting module is operational at the level of senior accounting units (postes comptables supérieurs) of the country; the preliminary version of the interface with SIGFIP is currently being tested at the ASTER level. The interface between SIGFIP and ASTER strengthens the linkages between fiscal and accounting operations and facilitates preparation of the general accounts of the financial administration, thereby shortening the time required to prepare the final budgets (lois de règlement). This is an essential operation to reinforce the expenditure chain. The auxiliary expenditure accounting module (CAD) will be operational in 2010. To press ahead with these reforms, a high-level information systems steering committee has been established within the Ministry of Economy and Finance.

The government adopted, by end-October 2009 (structural benchmark), all the necessary provisions to transfer FSIPP (Fonds de Sécurisation des Importations en Produits Pétroliers) / FSAPP (Fonds de Sécurisation des Approvisionnements en Produits Pétroliers) collection from SAR to the DGID and ensure transparent monitoring and improved accounting. The DGID initiated control over FSAPP in October 2009, in particular with respect to the financial flows between SAR and other oil companies. To this end, since November 2009: (i) FSAPP revenues related to imported finished petroleum products have been collected by the DGID directly from oil companies and deposited in a Treasury account; (ii) FSAPP revenues related to refinery operations have been collected by SAR and transferred to the DGID, which will deposit the funds in a Treasury account at the BCEAO; (iii) FSAPP revenues collected on refinery operations are being used to pay the balance of SAR’s debt and for investments in the petroleum sector and SAR; and (iv) any subsidy or transfer to SAR, or any strategic investment in the petroleum sector considered important by the government (such as strengthening SAR’s refinery capacities, installing the sea line, etc.) will need to be transparently reflected in the government budget and be subject to public procurement rules.

III. MACROECONOMIC POLICIES FOR THE REMAINDER OF 2009 AND FOR 2010

A. Outlook

6. **Improvements in the global economic outlook should help support a gradual recovery in economic activity in Senegal.** Growth of about 3½ percent is expected in 2010. The projection assumes that the global recovery will continue. Inflation is expected to return to about 2 percent as oil and food prices cease to exert downward pressure on consumer prices.

7. **These projections are subject to substantial risks.** Unfavorable developments in the international environment, including a decline in private transfers from abroad, official
development assistance, exports, or foreign direct investment would have a negative impact on economic growth. Also, energy sector issues will need to be resolved fast to minimize risks of a growing adverse impact on economic activity.

B. Fiscal Policy Stance

8. The global financial crisis and ongoing challenges in the energy sector affected budget developments in 2009. In light of weak revenues, the government contained expenditure taking into account available resources. The government benefited from a ten-year CFA franc loan from the BCEAO equivalent to the SDR allocation, but some expected financing failed to materialize, including privatization receipts (Hotel Méridien). The basic fiscal deficit will remain within the quantitative assessment (performance) criterion at end-December 2009 (CFAF 119 billion).

9. For 2010, the budget submitted to the parliament in October is generally in line with the macroeconomic framework of the Third Review. Given the effect on revenues of an economy operating below potential, the overall budget deficit (including grants) could reach about 5 percent of GDP in 2010. The budget aims to increase capital expenditure to about 11 percent of GDP and to protect social outlays. In the current challenging economic environment, it is essential to protect social expenditure. Accordingly, it will be increased from 33 percent at end-2008 to 35 percent of total expenditure in 2010. The government will make every effort to rapidly increase social expenditure further to the PRSP target of 40 percent of total expenditure, initially set for 2010.

10. The government has managed to eliminate payment delays in the regular expenditure chain and is committed to settling, swiftly and transparently, all extrabudgetary arrears and public institution and agency debt identified in the recent audit. It is in the process of specifying the settlement procedures.

(a) The government will issue a press release summarizing the results of the audit of extrabudgetary expenditure and public institution and agency debt, setting forth its strategy for settling payments in the first supplementary budget for 2010, and clearly describing the modalities for settlement (structural benchmark, January 31, 2010).

(b) A supplementary budget will be submitted to parliament no later than May 15, 2010 (structural benchmark, May 15, 2010). It will include the specific entries/items authorizing the Ministry of Finance to settle in 2010 the extrabudgetary arrears and the public institution and agency debt identified in the July 2009 audit, and not yet budgeted for. Debts not requiring a budgetary allocation will be presented in an annex to the supplementary budget. In the event financing falls short of what the budget requires, trade-offs will be necessary. Furthermore, the government will ensure that transfers from Treasury correspondent accounts (held by agencies
and public institutions) are made in a timely manner (no later than 90 days after the Treasury receives the check) to their bank accounts and/or as payments to enterprises for bills, invoices, and other statements that have fallen due. These provisions apply to checks awaiting Treasury approval as of December 17, 2009. Those checks for which the 90-day period has passed will be settled by end-September 2010 in accordance with a specific plan. Accordingly, the following steps will be taken: (i) a cash flow plan is established in advance between the Treasury and the correspondents, and this plan is updated periodically; (ii) transfer or payment intentions are reported to the Treasury at least thirty days before the withdrawal or payment date. To support this process, the government will adjust the timing of transfers to Treasury correspondent accounts as needed.

11. The government commits to settle at least 50 percent of extrabudgetary arrears and public institution and agency debt identified in the July 2009 audit, in accordance with the strategy announced by the government in January (structural benchmark, end-September 2010). Additional resources available in 2010 will be used for payment of the remaining amounts.

12. **In order to mobilize sufficient financing, debt management will be strengthened in line with the government’s prior commitments.** The government will update the rolling two-year government issuance calendar on a quarterly basis or after each issuance, in cooperation with the Central Bank of West African States (BCEAO). The government will signal to the WAEMU Council of Ministers the need to improve coordination of Member States’ access to the regional financial market.

13. **The government bases its medium-term fiscal policy stance on debt sustainability considerations, and it will maintain a prudent fiscal policy.** It is committed to limiting the overall fiscal deficit to 4 percent of GDP over the medium term. The government’s semi-annual public debt sustainability analysis will include a risk assessment for contingent liabilities arising from guarantees issued by the government to Public-Private Partnerships (PPPs) and operations of public enterprises.

14. **To ensure the debt remains sustainable, the government will focus on concessional financing and, in general, not contract or guarantee external borrowing on nonconcessional terms.** To supplement resources from donors and the private sector, external non-concessional funds earmarked for the Dakar-Diamniadio toll highway and authorized by the program are being mobilized. The government requests to raise the existing ceiling for non-concessional borrowing for this project from CFAF 80 billion (quantitative assessment (performance) criterion) to CFAF90 billion. The higher ceiling would allow the government to accommodate possibly higher costs and issue a bond in international markets of US$200 million, typically seen as a minimum size for this type of transaction. The small increase would have no negative impact on debt sustainability. The government will consult with IMF staff in advance regarding any other exceptions to this program criterion. Nonconcessional borrowing should be guided by
debt sustainability considerations and should be linked to specific economically profitable projects, for which sufficient concessional financing could not be mobilized.

C. Structural reforms

Budget Reforms

15. **With progress made, the government remains committed to continuing its ambitious budget reforms.** These reforms, based on a fiscal reform program supported by the government and development partners (in particular the IMF technical assistance report and the PEFA report) are essential to enhancing budget efficiency and transparency, while also helping to protect macroeconomic stability.

16. **As during the last budget cycle, the government will follow the closing provisions for budget execution and accounting.**

(a) The government has set a November 30 cut-off date for making budget commitments (engagements).

(b) The legally stipulated complementary period, under which the administrative phase of budget execution (payment orders) ends on December 31 (structural benchmark) and the accounting phase (payments) at end-February of the subsequent year, will be applied.

(c) Beyond February 28, any operation from the previous budget year with an impact on government cash flows must be included in the accounts for the current year.

(d) The SIGFIP data for each budget year will be frozen and published in detail on a website of the Ministry of Economy and Finance latest by April 30. For any payment after April 30, a new payment order needs to be issued and imputed to the current fiscal year. A payment of CFAF 5 billion, still outstanding when the accounting for the 2008 budget was closed, should have been recorded in the 2009 Treasury accounts but was recorded retroactively in 2008. Unwinding this transaction would have been too cumbersome administratively.

(e) The preliminary SIGFIP and TOFE end-month data will be published on a website of the Ministry of Finance within 10 and 45 days, respectively, beginning with the TOFE for November 2009 and the SIGFIP for end-December 2009.

17. **To facilitate timely budget closure the government will clear Treasury suspense accounts.** The suspense accounts on the books of the Treasury will be cleared to the extent that available information allows, in an effort to reduce transactions in suspense accounts to a strict minimum by end-February. This will allow timely closure of Treasury accounts, which, in the past, were not finalized until several years after the end of the budget year.
18. **The government will make every effort to improve SIGFIP as a key budget monitoring system, and to this end will implement the recommendations of the IMF PFM TA missions.** Following the audit of SIGFIP, and the two PFM TA missions in late 2008 focusing on the expenditure chain and budget execution, the government has requested follow-up technical assistance from the IMF, which is tentatively scheduled for February 2010. In the short term, the government intends to extend SIGFIP to cover all operational line ministries. The government intends to improve SIGFIP by incorporating payroll expenditure and implementing the SIGFIP-ASTER interface (structural benchmark, end-July 2010).

19. **The compilation of draft budget reviews will continue.** The draft budget review law for 2008 will be forwarded to the Audit Court by end-December 2009 and the one for 2009 by end-September 2010.

20. **To improve its cash management, the government has conducted a census of all government accounts, including of public institutions and agencies, with a view to setting up a strategy to establish a single Treasury account.** This was carried out by the Financial Audit Inspectorate (*IGF*) in 2006 and will be updated. All administration, public institution and agency accounts, including their bank accounts, will be listed. The list will be exhaustive. It will include for each account the number, name of the holder, and the balance as at December 31, 2008 and 2009 (structural benchmark, July 2010). To ensure that the census is comprehensive, the government will ask ministries and public institutions and agencies for a list of accounts and permission for their banks to provide the necessary information to the Treasury. This census is a significant step toward establishing a single Treasury account, which is an essential tool for improving daily liquidity management of the central government.

**Tax Administration**

21. **The strong performance of the Senegalese tax system must be preserved.** The resolution of the government’s payment delays and transfer of direct tax collection from the Treasury to the DGID should strengthen revenue collection. While revenues have come under pressure mainly because of the financial crisis, the tax administration authority will intensify its revenue collection efforts.

22. **Following the analysis of tax expenditures, the government will implement the following measures, with the aim of incorporating the first changes in the 2011 budget.**

(a) Establish an action plan designed to eliminate ineffective and/or inefficient tax expenditures with a significant budgetary cost. The study of tax expenditures aimed at providing a basis for enhancing the fairness, performance, and integrity of the tax system. Taking into account costs and benefits, the action plan will identify the key measures that could be eliminated and will review the legislative or regulatory amendments required for their abolition (structural benchmark, March 2010).
(b) Beginning January 1, 2010, carry out an ex ante impact assessment prior to any adoption of new tax expenditures. The aim is for the central government to establish a measure’s effectiveness and efficiency prospectively, prior to adoption, and to not adopt the tax expenditure otherwise. This is essential to achieve the rationalization referred to in (a).

(c) By October 15, 2010, incorporate into one single document the general tax code and all legislation governing domestic taxation. The study of tax expenditures has shown that they are many and various and dispersed among several laws contained in different documents. In the interest of simplicity and effectiveness, it is advisable to consolidate all rules and regulations pertaining to domestic taxation into one single document (structural benchmark, October 31, 2010).

Energy Sector

23. **Following the surge in oil prices between 2005 and 2008, and the resulting financial impact on SENELEC, major reforms were initiated by the government in collaboration with donors.** In 2008, the authorities adopted a letter of development policy for the energy sector, designed to ensure a quality energy supply at lowest cost. The reform of the energy sector is supported by a range of donors, specifically, the World Bank and the Agence Française de Développement (AFD). This letter focused on the financial rehabilitation of the electricity sector, the institutional reform of SENELEC in the medium term, and the strengthening of governance. The sector reform plan had identified a financing requirement in the amount of CFAF 109 billion. The government participated in 2007 in the amount of CFAF 65 billion and the World Bank and AFD disbursed an initial tranche in the amount of CFAF 37 billion in 2008 in the form of budgetary assistance, of which CFAF 15 billion remains to be disbursed (CFAF 6 billion in additional recapitalization, and CFAF 9 billion in subordinated equity loans).

24. **Despite ongoing reforms in the energy sector, which are critical to raise Senegal’s growth prospects, the situation remains very challenging.** Frequent electricity outages in August 2009 due to SENELEC’s strained cash-flow situation led to breakdowns in electricity production. In early September 2009, the World Bank and the AFD sent an emergency mission to assess the situation. The mission and the government identified several reasons explaining the situation that arose in August, specifically, (i) technical faults (GTI, Kounoune, TAG2, TAG3) that greatly increased the costs of production; (ii) a recurrent pricing mismatch (as well as a government compensation for 2008 which had not been paid in full); (iii) commercial and operational performance below budget expectations; (iv) significant constraints relating to fuel supplies; (v) delays in implementing a policy to manage demand; (vi) stocks of arrears and debt servicing that place a heavy burden on cash flow; and (vii) continued cash flow problems and insufficient internal warning systems reflecting persistent weaknesses in the company’s governance framework. These problems have slowed the rate of SENELEC’s financial stabilization despite the fall in the level of arrears from approximately CFAF 100 billion at end-
December 2008 to CFA 70 billion at end-September 2009, comprising: CFA 44 billion with central government, including CFAF 12 billion in VAT suspended and not due; as well as CFAF 30 billion with its private suppliers and creditors.

25. **The government, in cooperation with the World Bank and the AFD, reviewed various reform scenarios and options.** The scenario that the government has chosen encompasses a comprehensive and consistent set of measures including the following:

(a) the restructuring of SENELEC’s short-term debt;

(b) implementation of the action plan to reduce nontechnical losses (improving performance) and costs (implementation of the cost reduction plan);

(c) improvement of business performance;

(d) prosecution of fraud;

(e) assessment of fuel supply and human resource management functions;

(f) the updating if necessary and implementation of the recommendations of the audit on financial and accounting procedures;

(g) the resolution of the problem relating to the private energy supplier GTI through the return to service of the power station and the revision of the contract, with support from financial, legal and technical assistance;

(h) the implementation of a detailed action plan to meet the conditions of the second tranches of budget support from the World Bank and the AFD relating to the restructuring of the sector;

(i) a tariff adjustment will be carried out by no later than April 1, 2010 in addition to other measures if necessary and in such a way as to avoid having a significant impact on vulnerable segments of the population;

(j) Quarterly price adjustments will be made, if necessary, in order to reflect variations in the costs of production or purchase of energy.

26. **The government, in agreement with the World Bank and AFD, is aware that the restoration of SENELEC’s long-term financial stability requires additional measures.** The government has decided on the following measures: (i) a debt-crossing agreement (*convention de dette croisée*) between the government and SENELEC; (ii) the rescheduling of on-lent debt (*dette rétrocédée*) of CFAF 17 billion and suspended VAT set at CFAF 12 billion over 60 months; (iii) an exemption from the VAT on new investments pursuant to the 2007-25 law; (iv) payment of the balance of CFAF 36 billion with respect to the 2008 compensation, and a
commitment to make appropriate provision in the 2011 and 2012 budget, allowing SENELEC to have access to its funds, specifically, CFAF 20 billion in 2010 and CFAF 16 billion in 2011, through the financial system. However, if warranted by exceptional circumstances, the government commits to taking appropriate and immediate steps to ensure the financial viability of the sector through a tariff adjustment or any other measure.

27. **In conclusion, the program is a coherent framework, aiming to enhance the subsector’s efficiency and financial sustainability in the short, medium, and long term.** The envisaged program should help, among other things, to reduce quasi-fiscal risks in a credible and sustainable manner, in particular by providing regular tax payments by SENELEC to the government. It will also provide for the completion of the unbundling of SENELEC’s activities (production, transportation, and distribution) and the increase in participation by the local and foreign private sector, consumers and workers in the capital of SENELEC, in accordance with the Letter of Development Policy for the sector as adopted by the government of Senegal.

**Financial Sector Reforms**

28. **The government recognizes that the financial sector is experiencing difficulties linked to domestic factors as well as the global crisis.** Nonperforming loans have increased and several banks continue to not meet selected prudential regulations. Against this background, the authorities are determined to make every effort to maintain stability in the financial sector. In particular, they undertake to:

(a) Continue to monitor closely, as part of their normal duties, solvency and liquidity in the banking sector, including by analyzing bank assets and liabilities, the nature and concentration of financing sources, liquidity relationships with parent companies or establishments from the same group abroad, and overall liquidity. They will also intensify exchanges with the WAEMU authorities and supervisors from foreign institutions with a presence in Senegal;

(b) Focus on macro-financial risks arising from financing linkages between the government, private sector, and financial system. Major banks will undergo regular stress tests. Consultations with the government and banks will be intensified to anticipate financing and cash requirements of the government and private sector;

(c) Closely monitor, in consultation with the central bank, the entry into force of the new minimum capital rules by end-2010;

(d) Further strengthen capacity and resources of the directorate in charge of regulation and supervision of microfinance institutions within the Ministry of Economy and Finance;

(e) Accelerate implementation of the recommendations of the Financial Sector Assessment Program (FSAP), jointly with WAEMU authorities. In this context, the authorities will
consolidate various reform initiatives and plans and prepare a consolidated action plan for Senegal by end-March 2010 (new structural benchmark). The action plan will take stock of progress since the 2004 national FSAP update and the 2007 regional FSAP. The action plan will determine priorities, assign key responsibilities, and include an indicative timetable for reform. Its coverage will be broad, and include measures for the banking sector, insurance sector, microfinance institutions, and other financial intermediaries, cash flow management, the legal environment, and access to financial services.

29. **The government will continue to improve the institutional, legal, and operational environment for private sector financing** to enhance household access to credit and financial intermediation. The following initiatives will be introduced:

(a) Implementation of an action plan to increase the rate of bank penetration to 20 percent by end-2012 through, *inter alia*, promotion of noncash means of payment by the government;

(b) Establishment of a supportive legal framework for credit information bureaus;

(c) Finalization of legislation governing venture capital to promote financing of start-ups and growth of innovative small- and medium-sized enterprises.

**Developing the private sector and improving governance**

30. **Raising growth requires fast implementation of the Accelerated Growth Strategy (AGS).** The government is determined to accelerate the momentum to improve the business environment and reach international standards. Senegal’s position in the World Bank’s Doing Business Indicators has fallen. Key areas for improvement include improving contract enforcement, reducing delays in transferring property rights, modernizing labor legislation, and simplifying customs procedures and access to finance. The government specifically commits to achieve the following as soon as possible:

(a) Improved efficiency in the commercial justice system, by providing courts with the resources required for the expeditious handling of economic disputes and through implementation of administrative measures already identified;

(b) Reduced delays in the transfer of property rights as specified in office memoranda issued in 2008, reduction in the cost of such transfers, and adoption and effective implementation of the circular from the Prime Minister regarding reductions in the time it takes to issue construction permits and hook up water, sanitation, electricity, and telephones;

(c) Extension of possibilities for renewing fixed-term labor contracts;

(d) Holding the second national forum on credit by end-March 2010, followed by implementation of its recommendations according to a timetable to be agreed.
31. **The government is also establishing various measures to improve governance as follows:**

(a) by the end of the first quarter of 2010, finalizing legislation on government property and real estate: (i) the law on real estate ownership and its implementation decree; (ii) updating of pricing scales for government-owned property;

(b) strengthening the Audit Court by providing it with the appropriate level of resources and promoting the training of judges with the help of donors;

(c) making sufficient sources of financing available for the procurement regulatory agency (ARMP).

**IV. PROGRAM MONITORING**

32. Quantitative assessment (performance) criteria (for end-December 2009 and end-June 2010) and quantitative indicators (for end-March 2010) were set to monitor program implementation in 2009-10 (see Table 1 below). Assessing progress and implementation of energy sector reform will be a focus of program reviews. The government and IMF staff also agreed on the structural benchmarks listed in Table 2 below. It is expected that the fifth PSI review, third ESF review and the next Article IV consultation will be concluded by May 28, 2010, and the sixth and last PSI review will take place by end-October 2010.
Table 1 of MEFP. Quantitative Assessment Criteria (Performance Criteria) and Indicative Targets for 2009-10 1/
(CFAF billions, unless otherwise specified)

<table>
<thead>
<tr>
<th>Assessment (performance) criteria</th>
<th>December 31, 2009</th>
<th>March 31, 2010</th>
<th>June 30, 2010</th>
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<td>Floor on the basic fiscal balance 2/</td>
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<td>Ceiling on the contracting or guaranteeing of new</td>
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<tr>
<td>Ceiling on government external payment arrears (stock) 4/</td>
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<tr>
<td>Ceiling on the amount of the float (depenses liquidees non payees par le Tresor) 6/</td>
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<td>Indicative target</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Quarterly ceiling on the share of the value of public sector contracts signed by single tender (percent)</td>
<td>20</td>
<td>20</td>
<td>20</td>
</tr>
</tbody>
</table>

1/ Indicative targets for March 2010, except for the assessment (performance) criteria monitored on a continuous basis.
2/ Defined as total revenue minus total expenditure and net lending, excluding externally financed capital expenditure, on-lending, HIPC and MDRI spending, and payment of extrabudgetary spending and agency debt identified in the July 2009 audit and included in the first supplementary budget of 2010. Cumulative since the beginning of the year. Total revenue excludes privatization receipts and sales of mobile telephone licenses.
3/ Excluding government or government-guaranteed CFAF borrowing from financial institutions within the WAEMU and external loans contracted by the airport project company (AIDB) to finance the construction of the new Dakar Airport.
4/ Monitored on a continuous basis.
5/ Cumulative since approval of second PSI review. The amount of up to CFAF 90 billion is to finance exclusively the Dakar-Diamniadio toll highway project.
6/ Defined as all expenditure for which a bill has been received and recognized (dépense liquidée) but not yet paid by the Treasury.
<table>
<thead>
<tr>
<th>Policy Measures</th>
<th>MEFP</th>
<th>Implementation date</th>
<th>Macroeconomic Rationale</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Stop issuing 2009 payment orders.</td>
<td>15</td>
<td>December 31, 2009</td>
<td>Improve transparency of budget execution and prevent recurrence of past budgetary slippages.</td>
</tr>
<tr>
<td>2. Issue a press release summarizing the results of the audit of extrabudgetary commitments and agency debt, the government’s strategy for settling payments in the first supplementary budget for 2010 submitted to parliament no later than May 15, 2010, and describing the settlement procedures.</td>
<td>10</td>
<td>January 31, 2010</td>
<td>Continue the normalization of financial relations with the private sector in a transparent fashion.</td>
</tr>
<tr>
<td>3. Draw up an action plan to suppress tax expenditures with a significant budgetary impact that are ineffective and/or inefficient, with the aim of incorporating the first changes in the 2011 budget.</td>
<td>21</td>
<td>March 31, 2010</td>
<td>Enhance the transparency of the tax system and increase revenues.</td>
</tr>
<tr>
<td>4. Prepare a consolidated action plan for implementing the FSAP recommendations.</td>
<td>27</td>
<td>March 31, 2010</td>
<td>Reduce the vulnerability and strengthen the development of the financial sector.</td>
</tr>
<tr>
<td>5. Submit to parliament a supplementary budget for 2010 that includes specific entries/items authorizing the Ministry of Finance to settle in 2010 the extrabudgetary arrears and public institution and agency debt identified in the July 2009 audit that have not yet been included in a budget. Any debt settlement not requiring a budget entry will be presented in an annex to the supplementary budget.</td>
<td>10</td>
<td>May 15, 2010</td>
<td>Complete the normalization of financial relations with the private sector.</td>
</tr>
<tr>
<td>6. Improve SIGFIP by including payroll expenditure and implementing the SIGFIP-ASTER interface.</td>
<td>17</td>
<td>July 31, 2010</td>
<td>Strengthen the monitoring of budget execution.</td>
</tr>
<tr>
<td>7. Conduct a census of all the accounts held by general government institutions, and include for each account the number, name of the holder, and the balance as of December 31, 2008 and 2009, with a view to adopting a strategy to establish a single Treasury account.</td>
<td>19</td>
<td>July 31, 2010</td>
<td>Improve the management of cash flows, as well as the transparency of operations.</td>
</tr>
<tr>
<td>8. Complete payment of at least 50 percent of extrabudgetary commitments and public institution and agency debt identified in the July 2009 audit according to the modalities of the strategy announced by the government in January.</td>
<td>10</td>
<td>September 30, 2010</td>
<td>Complete the normalization of financial relations with the private sector and improve the business climate.</td>
</tr>
<tr>
<td>9. Incorporate in a single document the general tax code and all legislation governing domestic taxation.</td>
<td>21</td>
<td>October 15, 2010</td>
<td>Further simplify the tax system.</td>
</tr>
</tbody>
</table>
ATTACHMENT II

TECHNICAL MEMORANDUM OF UNDERSTANDING

Dakar, December 4, 2009

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

I. PROGRAM CONDITIONALITY

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

II. DEFINITIONS, ADJUSTERS, AND DATA REPORTING

A. The Government

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

B. Basic Fiscal Balance (Program Definition)

Definition

4. The basic fiscal balance (program definition) is the difference between the government’s budgetary revenue and total expenditure and net lending, excluding externally-financed capital expenditure (financed by donors), drawings on on-lent loans (except on-lent loans to the energy sector financed through donor budget support), expenditure funded with HIPC- and MDRI-related resources, and expenditure related to the settlement of agency debt and extrabudgetary arrears identified in the July 2009 audit and included in the first supplementary budget for 2010. Budgetary revenue excludes privatization receipts and sales of mobile telephone licenses or other government assets. Government expenditure is defined on the basis of payment orders accepted by the Treasury (dépenses prises en charge par le
Trésor). The assessment (performance) criterion is set as a floor on the cumulative basic fiscal balance since the beginning of the year.

Example

5. The floor for the basic balance (program definition) as at June 30, 2010 is minus CFAF 59 billion. It is calculated as the difference between budgetary revenue (CFAF 621 billion) and total expenditure and net lending (CFAF 851.5 billion), excluding externally financed capital expenditure (CFAF 136.5 billion), drawings on on-lent loans (CFAF 5 billion), and expenditure funded with HIPC- and MDRI-related resources CFAF 30 billion).

Reporting requirements

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

C. Budgetary Float

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

Reporting requirements

7. The authorities will report to Fund staff on a weekly basis (i.e., at the end of each week), and at the end of each month, a table from the expenditure tracking system (SIGFIP) showing all committed expenditures (dépenses engagées), all certified expenditures that have not yet been cleared for payment (dépenses liquidées non encore ordonnancées), all payment orders (dépenses ordonnancées), all payment orders accepted by the Treasury (dépenses prises en charge par le Trésor), and all payments made by the Treasury (dépenses payées). The SIGFIP table will exclude delegations for regions and embassies. The SIGFIP table will also list any payments that do not have a cash impact on the Treasury accounts.
D. Spending Undertaken Outside of Simplified and Normal Procedures

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

9. The authorities will report to Fund staff on a monthly basis and with a maximum delay of 30 days any such procedure, together with the SIGFIP table defined in paragraph 8.

E. Government External Payment Arrears

Definition

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

Reporting requirements

11. The authorities will promptly report to Fund staff any accumulation in external payment arrears.

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

Definition

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

(i) CFAF debt contracted or guaranteed by the government with WAEMU residents;

(ii) CFAF debt initially contracted or guaranteed by the government with WAEMU residents subsequently acquired by nonresidents;

(iii) CFAF government or government-guaranteed debt where the agreement is between the government and a resident WAEMU entity and there is no ensuing contractual obligation
between the government and a nonresident entity, regardless of whether the resident WAEMU entity resells the debt to a nonresident;

(iv) debt rescheduling transactions of debt existing at the time of the approval of the PSI; and

(v) external debt contracted by the airport project company (AIDB) to finance construction of the new Dakar Airport.

13. This criterion is measured on a cumulative basis since the approval of the second program review and applies continuously. The ceiling is raised to accommodate CFAF 90 billion to finance exclusively the Dakar-Diamniadio toll highway project. No adjuster will apply to this criterion.

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

15. Any external debt of which the present value, calculated with the reference interest rates mentioned hereafter, is greater than 65 percent of the nominal value (grant element of less than 35 percent) is considered nonconcessional, with the exception of IMF lending. For debt with a maturity of more than 15 years, the ten-year reference market interest rate, published by the OECD, is used to calculate the grant element. The six-month reference market rate is used for debt with shorter maturities.

Reporting requirements

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

G. Public Sector Contracts Signed by Single Tender

Definition

17. Public sector contracts are administrative contracts, drawn up and entered into by government entities subject to the procurement code, for the procurement of supplies, delivery of services, or execution of work. Public sector contracts are considered single-tender contracts when the contracting agent signs the contract with the chosen contractor
without competitive tender or award. The quarterly indicative target will apply to public sector contracts examined by the Direction Centrale des Marchés Publics (DCMP).

Reporting requirements

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

III. ADDITIONAL INFORMATION FOR PROGRAM MONITORING

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

   (a) Effective immediately: any decision, circular, edict, decree, ordinance, or law having economic or financial implications for the current program;

   (b) With a maximum lag of 30 days, preliminary data on:

      • Tax receipts and tax and customs assessments by categories, accompanied by the corresponding revenue;
      • The monthly amount of expenditures committed, certified, and for which payment orders have been issued;
      • The quarterly report of the Debt and Investment Directorate (DDI) on execution of investment programs;
      • The monthly preliminary government financial operations table (TOFE), based on the Treasury accounts (balances de compte);
      • The provisional balance of the Treasury accounts; and
      • A reconciliation table between the SIGFIP table and the Treasury accounts, between the Treasury accounts and the fiscal reporting table (TOFE) for revenues, and between the Treasury accounts and the fiscal reporting table (TOFE) for total expenditure and net lending and between the TOFE and the net government position (NGP), on a quarterly basis.

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

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

21. The government will report to Fund staff:

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

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