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Guinea-Bissau: Supplementary Letter of Intent, Supplementary Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding

April 29, 2011

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SUPPLEMENTARY LETTER OF INTENT

Bissau, April 29, 2011

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

Dear Mr. Strauss-Kahn,

1. This letter of intent and the attached memorandum of economic and financial policies (MEFP) update and supplement our correspondence of November 16, 2010, and describe performance under the government's economic program since then.
2. The government's economic program, supported by a three-year Extended Credit Facility (ECF), is on track. All performance criteria through end-December 2010 have been observed, and structural benchmarks for the second review were met. All quantitative targets for end-December were also met, including the one on social and priority spending (see Tables 1 and 2 of the MEFP).
3. The attached MEFP reflects the government's commitment to the goals of achieving fiscal and external sustainability, reviving economic growth, reducing poverty, and making progress toward the Millennium Development Goals (MDGs). The government believes that the steps taken and economic policies it intends to pursue in the remainder of 2011 are adequate to achieve the targets and objectives under the program (performance criteria and structural benchmarks for the third and fourth review are included in Tables 3 and 4 of the MEFP). However, if necessary, the government will adopt additional measures to achieve these objectives. It will consult with the Fund before adopting such measures or if there are changes in the policies contained in the MEFP, in accordance with the Fund's policies on such consultations.
4. In view of the performance under the ECF-supported program and the government commitment to economic reforms as specified in the MEFP attached, the Government of Guinea-Bissau requests completion of the second review and the third disbursement under the ECF arrangement of SDR 2.414 million.
5. In line with our commitment to transparency, we request the IMF to publish this letter of intent, the attached MEFP, the Technical Memorandum of Understanding, and the staff report relating to this request.

Sincerely yours,

/S/

José Mario Vaz
Minister of Finance

ATTACHMENT I. SUPPLEMENTARY MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES FOR 2011

I. INTRODUCTION

1. **This memorandum updates the MEFP of November 16, 2010, and summarizes the progress achieved since then.** The program objectives are unchanged: achieving fiscal and external sustainability, reviving economic growth, and making progress toward poverty alleviation and the Millennium Development Goals (MDGs).
2. **Program implementation has taken place against the background of rising import prices for food and fuel prices.** The government considers that adjustment is preferable to accommodation in light of the permanent nature of the price shock and the need to secure a full pass-through of price changes over time to encourage consumers and producers to adjust.

II. RECENT DEVELOPMENTS AND PERFORMANCE UNDER THE PROGRAM

A. Economic Developments in 2010

3. **Macroeconomic performance improved, owing to a rebound in the price of cashew exports and improved liquidity in the banking system.** Strong terms-of-trade gains more than offset a weather-related decline in the cashew harvest. Overall, growth accelerated slightly to 3.5 percent in 2010, up from 3.0 percent in 2009. Driven by rising import prices for food and fuel, headline inflation accelerated from -1.6 percent in 2009 to 1.1 percent in 2010, still below the WAEMU convergence criterion. The external current account deficit, excluding official transfers, narrowed by about 4 percentage points of GDP.
4. **The government adjusted to a shortfall in budget support of 3.2 percent of GDP (or CFAF13.4 billion).** Fiscal adjustment was achieved through higher revenue (0.5 percentage points of GDP) and lower spending (2.1 percentage points of GDP), while the government drew down part of its deposits at the BCEAO (0.6 percent of GDP). Higher than programmed revenue reflected tighter controls at customs and revenue administration and more than offset lower disbursements in fishing compensation. The government contained spending through lower outlays on goods and services and underexecution of the public investment program.

B. Performance Under the ECF Program

5. **Despite the shortfall in budget support, fiscal performance has been satisfactory.** All performance criteria and indicative targets at end-December 2010 were met (Table 1).
6. **All structural benchmarks for the second review have been met.** The government made the link from the treasury to customs administration operational; submitted to the

council of ministers the action plan for public administration reform; and began to use the unified payroll system at the ministries of finance and labor and public administration (Table 2). Progress on other structural measures is detailed in Table 4.

III. MACROECONOMIC OUTLOOK AND ECONOMIC POLICIES FOR 2011

A. Macroeconomic Outlook

7. **The growth outlook is broadly unchanged.** Economic growth is expected to accelerate moderately to 4.3 percent in 2011, driven by rising cashew production, higher cashew prices, and a steady rebuilding of infrastructure, especially roads, electricity, and water. Risks to the outlook would seem to be fairly balanced: downside risks arise from higher-than-expected import prices for food and fuel while there is an upside from higher-than-projected cashew prices in line with recent cashew trading elsewhere.

8. **Inflation prospects worsened, reflecting rising import prices of food and fuel.** Headline inflation is now projected at 4 percent, above the WAEMU convergence criterion. However, core inflation is expected to remain subdued, and headline inflation should come back within the WAEMU convergence criterion range in 2012, once the one-off effect of rising import prices subsides.

B. Fiscal Policy

9. **The government remains committed to strengthening public finances.** Fiscal policy will focus on containing the domestic primary deficit in line with available financing; sustaining efforts to mobilize more revenue; and keeping tight spending controls.

10. **The government has secured budget support beyond what has been budgeted for in 2011 and plans to restore public investment under the program.** In early March, the government received a new grant from the Angolan government of US\$12 million (about CFAF6 billion or 1.3 percent of GDP) to finance capital spending. The government decided to allocate the new grant received from Angola to finance investments in road and agriculture projects. The government held consultation with the EU under the agreement of Cotonou on March 29, and the EU announced it will condition its resumption of support to Guinea-Bissau on the undertakings by the government in the coming months in several areas, including security sector reform and appointments of military personnel. At the same time, the budget support operations assumed in the program from the World Bank (CFAF3.6 billion) and the African Development Bank (CFAF3.9 billion) are moving forward, with disbursements expected in the second half of the year.

11. **The government will secure a full pass-through of import price changes over time to encourage consumers and producers to adjust.** In early-March, the government reduced duties on fuel products with a view to mitigate the impact on the cost of living, but

reversed the measure in end-March, after considering the expected permanent nature of the oil price shock and the need to adjust rather than accommodate the shock.

12. The government will introduce a strong package of measures to reinforce fiscal revenues this year and prepare the ground to sustain gains in revenue mobilization next year. In addition to restoring the reference price of diesel for customs purpose back to levels that prevailed in early March (CFA 301.68), the government will:

- i. adjust the reference price for imported sugar up to market levels by end-April;
- ii. adjust the reference price for imported diesel from CFAF301.68 to CFAF373.68 by end-June;
- iii. refrain from reducing reference prices for customs purposes;
- iv. ensure that the commission for regular adjustment of domestic fuel prices holds monthly meetings to enforce that domestic prices reflect changes in international prices;
- v. review the reference prices of rice, flour, diesel, and cashew until the end of the year, with a view to raise them closer to market levels, as part of the 2012 budget; and
- vi. reduce or eliminate customs exemptions identified by the current government's review (see below).

C. Structural Reforms

13. The government will renew efforts to consolidate gains and sustain its reform agenda as detailed in the MEFP of November 2010 (Tables 3 and 4).

14. The new five-year poverty reduction strategy (PRS) will be submitted to the Council of Ministers by June. The government's medium-term economic reform program supported under the ECF arrangement is in line with the new PRSP. To implement the strategy, the government will coordinate with donors and development partners. Priorities are to identify economic projects in line with the PRS, ensure adequate coordination with donors in support of that strategy, and implement the PIP.

15. In what follows we provide an update of progress on economic reforms and the way forward.

(i) Strengthening Revenue Collection

16. The government is on track with modernizing and improving customs and tax administration:

- a. On customs, the government will (i) finish customizing and testing the ASYCUDA ++ system with the parameters for Guinea-Bissau and train staff with the help of UNCTAD; and (ii) finish the comprehensive review of all custom exemptions to further broaden the customs revenue base.

- b. On tax administration, the government prepared an action plan (with TA from WEST AFRITAC building on the FAD mission of last September) to: (i) revise taxpayer segmentation based on turnover criteria, with thresholds for small and large taxpayers at CFAF10 and 40 million, respectively; (ii) cross-check ASYCUDA data with tax returns for 300 largest importers in 2009–10; and (iii) audit importers underreporting tax liabilities, beginning with largest gaps. A newly set up team at Department of Internal Taxes (DGCI) will lead efforts in this area, with a view to introduce a VAT system by 2013.

(ii) Modernizing the Public Administration and Creating Space for Priority Spending

17. **In March, the Council of Minister approved the medium-term action plan for the reform of the public administration, to make it more modern and efficient.** While the reform is gradual and figures will be finalized only after the unification of the payroll system, the plan is to reduce the size of the civil service from over 16,000 in 2010 to about 14,000 by 2015, with a view to start bringing the ratio from 10 to 6-7 employees per 1000 inhabitants in line with the norm in the WAEMU region.

18. **The government has made progress implementing stricter payroll controls and a comprehensive database.** The government began using the unified payroll system in the ministries of finance and public function in March, and will start using the system in all ministries by August. The government has started implementing the personnel management (SIGRHAP), which is expected to be operational by end-August.

19. **The government is working with partners to implement defense and security sector reform (SSR).** Following a decision by the European Union (EU) not to deploy a new mission to monitor the implementation phase of the SSR, the government strengthened coordination with the United Nations Integrated Peace-Building Office in Guinea-Bissau (UNIOGBIS) and regional and bilateral partners, including ECOWAS and the Community of Portuguese Language Countries (CPLP), to prepare a plan to ensure adequate financing of the reform, especially of the pension fund. The UN announced in February its Priority Plan for Guinea-Bissau with an allocation of US\$16 million for civilian-led aspects of the security sector reform. In March, the Council of Ministers approved the ECOWAS-CPLP road map for the SSR.

(iii) Removing Impediments to Private Sector Development

20. **The government will intensify efforts to prepare an action plan that removes impediments to private sector development and improves the ease of doing business in Guinea-Bissau.** The government will also cooperate with the World Bank to prepare a plan to manage the country's natural resources by December.

(iv) Reinforcing Debt Management and Arrears Clearance

21. **In the wake of the HIPC completion point in December, the government will seek to reinforce its debt management.** With the assistance of UNCTAD, the Public Debt Office plans to hire and train new staff, start producing quarterly electronic reports on public debt by June 2011, and start using SYGADE by December to record, monitor, and manage all public debt. UNCTAD has begun providing training for government staff on SYGADE.

22. **The government has requested a deferral of payment and better terms on debts owed to the Central Bank of West African States (BCEAO).** The renegotiation of the debt owed to the BCEAO (about CFAF90 billion or 20 percent of GDP) has been suspended until a new BCEAO governor is appointed. The debt with the BCEAO stems from several sources: a required capital contribution to join the WAEMU; debt from the BCEAO's repayment, on behalf of the government, of previous IMF credit to Guinea-Bissau; and the on-lending of the SDR allocation.

23. **The government will continue with its medium-to-long term arrears clearance strategy of making annual payments consistent with available resources.** A team of independent auditors issued a preliminary audit report for 2000-07 arrears. The government is verifying the audit with a view to incorporate verified arrears into its arrears strategy.

D. Financial Sector and Monetary Policies

24. **Monetary policy will continue to be pursued within the WAEMU framework.** This arrangement has enabled Guinea-Bissau to contain inflation and maintain a stable exchange rate. As the rise in import prices for fuel and food wears off, domestic inflation is expected to return within the WAEMU target by 2012.

E. Post-HIPC Completion Point Work

25. **The government is taking steps to implement the HIPC completion point.** It has asked all creditors to confirm their intention to provide HIPC and topping up debt relief. The government received topping up assurances from Portugal, thus reaching the 80 percent commitment threshold necessary for the World Bank to proceed with topping up and MDRI assistance. Negotiations with the Paris Club are now expected to take place in May.

F. Capacity Building and Technical Assistance

26. **The government has identified technical assistance priorities in revenue administration, tax policy, and debt management.**

- **Revenue administration:** In 2010, a FAD technical assistance (TA) mission performed an assessment and made recommendations for the government to strengthen revenue administration. The government will implement these recommendations with technical

assistance from the regional AFRITAC and will seek further technical assistance from FAD.

- **Tax policy:** The government plans to introduce a value-added tax (VAT) by 2013, in line with other WAEMU countries. Initial steps and technical assistance are needed to support the design, preparation, and implementation of the VAT.
- **Debt management:** Although its external debt outlook has improved significantly since debt relief, debt management has emerged as an urgent new priority. The government will seek technical assistance to strengthen public debt management, including the public debt unit at the Ministry of Finance, so that it can record and manage all public debt and produce quarterly reports on public debt.

G. Program Monitoring

27. **The second year of the program covers the 12 months from January 1, 2011, to December 31, 2011.** The program will be monitored using quarterly quantitative indicators and structural benchmarks, as well as semiannual reviews and the quantitative performance criteria presented in Table 3. Tables 4 and 5 contain a list of structural measures identified by the government, including the structural benchmarks for the third and fourth review. The definitions of quantitative performance criteria and benchmarks are in the attached TMU. The government expects the third review to take place in December 2011 and the fourth review is expected to take place in May 2012.

Table 1. Guinea-Bissau: Quantitative Indicators for the ECF Program for 2010

Quarterly Targets ¹
(Cumulative, CFAF millions)

	End-March		End-June		End-Sept.		End-Dec.	
	Prog. ²	Actual	Prog. ²	Actual	Prog. ²	Actual	Prog. ²	Prel.
Performance criteria³								
1. Domestic financing of the budget	10,618	5,975	8,627	302	8,736	4,308	12,231	3,409
2. New domestic arrears	0	0	0	0	0	0	0	0
3. External nonconcessional public borrowing, maturity > 1 year	0	0	0	0	0	0	0	0
4. External short term public borrowing	0	0	0	0	0	0	0	0
5. New external payment arrears	0	0	0	0	0	0	0	0
Indicative targets								
6. Government tax revenue	5,420	6,391	15,148	17,538	24,218	25,394	30,101	33,086
7. Domestic primary balance (commitment basis)	-7,789	-2,401	-8,386	1,048	-11,030	-1,352	-17,938	-4,865
8. Nonregularized expenditure (DNTs)	200	0	200	0	200	0	200	0
9. Social and priority spending	4,062	1,989	8,123	4,223	12,185	6,818	8,647 ⁴	9,152

¹ Cumulative from January 1. The definition of the aggregates and adjustors is provided in the Technical Memorandum of Understanding (TMU).

² Adjusted target under the program.

³ Performance criteria (PC) are defined for June and December. March and September are indicative. All performance criteria (PC) are ceilings and PC 3, 4, and 5 apply continuously.

⁴ Indicative target for social and priority spending was revised compared to program (IMF Country Report No. 10/379) from CFAF 16,246 to CFAF 8,647.

**Table 2. Guinea-Bissau: Structural Benchmarks Under the ECF
Second Review**

Category		Structural Benchmarks	Macro Rationale	Actual Delivery Date	Ministry	Status of Implementation
Second Review						
Fiscal management	1	Establish an operational link from budget/treasury under the SIGFIP to the customs and tax administration.	Greater control in budget execution	March 2011	MoF ¹	Met
Expenditure reforms	2	Submit to the Council of Ministers an action plan for public administration reform, with a medium-term schedule to downsize the civil service through retirement and removing redundant workers beginning in 2011.	To improve the efficiency of civil service	Jan 2011	MoF MinLaPS ²	Met
	3	Start using the unified payroll and personnel management system and pilot it in the Ministries of Finance and Labor and Public Administration.	To modernize public administration	Jan 2011	MoF MinLaPS	Met

¹ Ministry of Finance

² Ministry of Labor and Public Administration

Table 3. Guinea-Bissau: Quantitative Indicators for the ECF Program for 2011

Quarterly Targets ¹
(Cumulative, CFAF millions)

	End-March	End-June	End-Sept.	End-Dec.
	Prog.	Prog.	Prog.	Prog.
Performance criteria²				
1. Domestic financing of the budget	1,431	-520	-1,954	0
2. New domestic arrears	0	0	0	0
3. External nonconcessional public borrowing, maturity > 1 year	0	0	0	0
4. External short term public borrowing	0	0	0	0
5. New external payment arrears	0	0	0	0
Indicative targets³				
6. Government tax revenue	6,437	17,988	30,506	37,917
7. Domestic primary balance (commitment basis)	-3,597	-5,842	-5,911	-12,087
8. Nonregularized expenditure (DNTs)	200	200	200	200
9. Social and priority spending	2,932	5,864	8,795	12,227

¹ Cumulative from January 1. The definition of the aggregates and adjustors is provided in the Technical Memorandum of Understanding (TMU).

² Performance criteria (PC) are defined for June and December. March and September are indicative. All PC are ceilings and PC 3, 4, and 5 apply continuously.

³ The indicative targets 6, 7 and 9 were revised compared to program (IMF Country Report No. 10/379) to reflect the higher revenue base from 2010 and the additional budget support.

Table 4. Guinea-Bissau: Structural Benchmarks Under the ECF
January 1, 2011–December 31, 2011

Category	Structural Benchmarks	Macro Rationale	Ministry	Status of implementation	
Third Review					
Tax reform and strengthening revenue collection	1	Customize and test ASYCUDA ++, and provide training to staff.	To strengthen revenue collection	MoF ¹	In progress
	2	Conduct a comprehensive review of all customs exemptions to broaden the customs revenue base and submit report to Council of Ministers.	To strengthen revenue collection	MoF	In progress
	3	Cross-check ASYCUDA data with tax returns for 300 largest importers in 2009–10.	To strengthen revenue collection	MoF	In progress
Expenditure reforms	4	Extend the computerized and unified payroll and personnel management system to all ministries.	To modernize public administration	MoF MinLaPS ²	In progress
Business environment	5	Prepare an action plan to identify and remove further impediments to private sector development and improve the ease of doing business in Guinea-Bissau.	Improve the ease of doing business	MinEcon ³	In progress
Public debt management	6	Start producing, on a quarterly basis, electronic reports on public debt (external and domestic).	Improve transparency	MoF	In progress
Fourth Review					
Public debt management	1	Use SYGADE to record, monitor, and manage all public debt (external and domestic)	Improve debt management	MoF	
Tax reform and strengthening revenue collection	2	Audit those importers underreporting their tax liabilities, beginning with largest gaps.	To strengthen revenue collection	MoF	
	3	Review the legal framework that regulates revenue sharing agreements (“restitutions”).	To strengthen revenue collection	MoF	
Business environment	4	Prepare a plan to manage the country’s natural resources.	Improve the ease of doing business	MinEcon	

¹ Ministry of Finance
² Ministry of Labor and Public Administration
³ Ministry of Economy

Table 5. Guinea-Bissau: Structural Measures for 2011

Category	Measures	Delivery Date
Tax reform & strengthening revenue collection	1 Raise reference price for cashew exports to US\$750 per ton.	2011
	2 Raise the reference price for staple imports (rice to CFAF6000, sugar to CFAF8500, and flour to CFAF8500).	2011
	3 Increase the tax rate on advance payment of the profit tax collected at customs (anticipation of industrial contribution) from 3 to 5 percent for the informal sector.	2011
	4 Reintroduce seals on alcoholic beverages and tobacco.	Jan 2011
	5 Customize and test the system of ASYCUDA ++ with the parameters for Guinea-Bissau (including the specific exemptions and tariffs), and train staff.	Aug 2011
	6 Restore the reference price for diesel for customs purpose back to early-March levels.	Apr 2011
	7 Adjust the reference price for imported sugar up to market levels.	Apr 2011
	8 Adjust the reference price for imported diesel from CFAF301.7 to CFAF373.0	Jun 2011
	9 Review price of rice, flour, diesel, and cashew, with a view to raise the reference price for these products to market levels by December 2011, to be incorporated in the 2012 budget.	Dec 2011
	10 Conduct a comprehensive review of all customs exemptions, with a view to reduce or eliminate identified exemptions.	Jun 2011
	11 Revise taxpayer segmentation based on turnover criteria, with threshold for small and large taxpayers at CFAF10 and 40 million, respectively.	Jun 2011
	12 Cross-check ASYCUDA data with tax returns for 300 largest importers in 2009-10.	Jun 2011
	13 Audit importers underreporting tax liabilities, beginning with largest gaps.	Dec 2011
	14 Increase to 90 percent large taxpayers filing rate for the general sales tax.	2011
	15 Continue to reinforce the large taxpayer unit in the Ministry of Finance.	2011
Fiscal management	16 Review the legal framework that regulates revenue sharing agreements ("restitutions") to increase the share of non earmarked revenues in the budget.	Dec 2011
	17 Seek technical assistance to reinforce budget preparation procedures.	Jun 2012
	18 Prepare and regularly updates the treasury plan for the 2011 budget.	2011
	19 Establish an operational link form budget/treasury under the SIGFIP to the customs and tax administration.	Mar 2011
	20 Continue publishing quarterly budget execution reports.	2011
	21 Modify the organic laws for the Audit Court.	2011
	22 Submit to Parliament the budgetary execution accounts for 2010.	Sep 2011

Civil service reform	23	Submit to the Council of Ministers an action plan for public administration reform, with a medium-term schedule to downsize the civil service through retirement and removing redundant workers beginning in 2011.	Jan 2011
	24	Start using the computerized and unified payroll and personnel management system in the Ministries of Finance and Public Service.	Jan 2011
	25	Extend the computerized and unified payroll and personnel management system to all ministries.	Aug 2011
Defense and security sector reform	26	Prepare an operational plan with a list of potential retirees and projects for the construction of military and security installations.	2011
Arrears clearance	27	Complete the audit of 2000–07 private sector arrears.	2011
Business environment	28	Adopt the implementing regulations of the new investment code.	2011
	29	Prepare an action plan to further identify and remove impediments to private sector development and improve the ease of doing business in Guinea-Bissau.	Aug 2011
	30	Prepare a plan to manage the country's natural resources.	Dec 2011
Social services	31	Adopt a new five-year poverty reduction strategy (PRS).	Jun 2011
Public debt management	32	Strengthen the unit of public debt management.	2011
	33	Produce quarterly electronic reports on public debt no later than three months after each quarter, in a manner consistent with the BCEAO reporting requirements.	Jun 2011
	34	Use SYGADE to record, monitor, and manage all public debt.	Dec 2011

ATTACHMENT II. TECHNICAL MEMORANDUM OF UNDERSTANDING

Bissau

April 29, 2011

1. **This memorandum updates the Technical Memorandum of Understanding of November 16, 2010 and describes the definitions of the quantitative and structural performance criteria, indicative targets, and structural benchmarks to monitor the program supported by an arrangement under the Extended Credit Facility (ECF). It also specifies the agreed periodicity and deadlines for transmission of data to IMF staff for program monitoring.**

Quantitative Indicators and Adjustors**A. Quantitative Indicators**

2. **The quantitative indicators are as follows:**
- a. Cumulative floors on government tax revenue
 - b. Cumulative ceilings on the domestic primary fiscal deficit (on a commitment basis)
 - c. Cumulative ceiling on the amount of nonregularized expenditures (DNTs).
 - d. Cumulative floor on social and other priority spending
 - e. Cumulative ceilings on the change in net domestic financing of the budget
 - f. Cumulative ceiling on new domestic arrears of the government, including wage arrears
 - g. Cumulative ceilings on new nonconcessional external debt contracted or guaranteed by the government
 - h. Cumulative ceiling on new external short term debt
 - i. Cumulative ceiling on new external payment arrears.

Quantitative indicators are set for end-March, end-June, end-September, and end-December. Quantitative performance criteria are proposed for end-June and end-December 2011 for indicators (e) through (i). Indicators for new nonconcessional external debt, new external short-term debt, and new external payment arrears are continuous.

Definitions and computation

3. **Government.** Unless otherwise indicated, “Government” means the central administration of the Republic of Guinea-Bissau and does not include any local

administration, the central bank, or any other public or government-owned entity with autonomous legal personality not included in the government flow-of-funds table (TOFE).

4. **The targeted floor on government tax revenues** includes direct and indirect taxes, as well as recovery of tax arrears and additional revenue efforts (Table 1).

Table 1. Quarterly Floors for Government Tax Revenues, 2011
(Cumulative, CFAF millions)

	March	June	Sept.	Dec.
	Prog.	Prog.	Prog.	Prog.
Tax revenues	6,437	17,988	30,506	37,917

5. **The domestic primary fiscal deficit on a commitment basis** is calculated as the difference between government revenue and domestic primary expenditure on a commitment basis (Table 2). Government revenue includes all tax and nontax receipts and excludes external grants. Domestic primary expenditure consists of current expenditure plus domestically financed capital expenditure, excluding all interest payments. Government commitments include all expenditure for which commitment vouchers have been approved by the Ministry of Finance; automatic expenditure (such as wages and salaries, pensions, utilities, and other expenditure for which payment is centralized); and expenditure by means of offsetting operations.

Table 2. Quarterly Domestic Primary Balance, New Domestic Arrears, and Nonregularized Expenditures, 2011
(Cumulative, CFAF millions)

	March	June	Sept.	Dec.
	Prog.	Prog.	Prog.	Prog.
Total domestic primary deficit	-3,597	-5,842	-5,911	-12,087
Revenue	7,813	21,253	39,449	49,860
Domestic primary expenditure	11,410	27,095	45,361	61,947
New domestic arrears	0	0	0	0
Nonregularized expenditures (DNTs)	200	200	200	200

6. **New domestic arrears of the government** are defined as accounts payable (rest-payer) accumulated during the year, still outstanding one month after the quarter for wages and salaries (including pensions), and three months after for goods and services and transfers, at end-March, end-June, end-September, and end-December 2011.

7. **Nonregularized expenditures** are defined as any treasury outlay not classified in the expenditure tables presented by the National Budget Directorate.

8. **Net domestic financing consists of bank and nonbank financing** (Table 3). Bank financing consists of net changes in the balances of the treasury accounts at the BCEAO (excluding net disbursement from the IMF) and commercial banks (excluding balances in those accounts that are not available for budget financing, such as accounts held under

double signature arrangements with donors) and in the outstanding amounts of loans, including T-bills, from the BCEAO and commercial banks, local and regional. Nonbank financing encompasses privatization receipts and any other financial debt held outside the banking system other than new domestic arrears.

Table 3. Domestic Financing by Quarter, 2011
(Cumulative, CFAF millions)

	March	June	Sept.	Dec.
	Prog.	Prog.	Prog.	Prog.
Domestic financing	1,431	-520	-1,954	0
Bank financing	1,431	-520	-1,954	0
BCEAO	1,431	-520	-1,954	0
Commercial banks (including regional)	0	0	0	0
Regional commercial banks and Treasury bills	0	0	0	0
Nonbank financing	0	0	0	0

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

9. **Definition of debt.** For the purposes of the relevant performance criteria, the definition of debt is set out in Executive Board Decision No.6230-(79/140), Point 9, as revised on August 31, 2009 (Decision No. 14416-(09/91)).

a. the term “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 sometime 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 lessee 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. For the purpose of the guideline, 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.

b. Under the definition of debt 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.

10. **Debt guarantees.** For the purposes of the relevant performance criteria, the guarantee of a debt arises from any explicit legal obligation of the government to service a debt in the event of nonpayment by the debtor (involving payments in cash or in kind).

11. **Debt concessionality.** For the purposes of the relevant performance criteria, a debt is considered concessional if it includes a grant element of at least 50 percent;¹ the grant element is the difference between the present value (PV) of debt and its nominal value, expressed as a percentage of the nominal value of the debt. The PV of debt at the time of its contracting is calculated by discounting the future stream of payments of debt service due on this debt.² The discount rates used for this purpose are the currency specific commercial interest reference rates (CIRRs), published by OECD.³ For debt with a maturity of at least 15 years, the ten-year-average CIRR is used to calculate the PV of debt and, hence, its grant element. For debt with a maturity of less than 15 years, the six-month average CIRR is used. The margins for differing repayment periods (0.75 percent for repayment periods of less than 15 years, 1 percent for 15 to 19 years, 1.15 percent for 20 to 29 years, and 1.25 percent for 30 years or more) are added to the ten-year and six-month CIRR averages.

12. **External debt.** For the purposes of the relevant performance criteria, external debt is defined as debt borrowed or serviced in a currency other than the CFA franc. This definition also applies to debt among WAEMU countries.

13. **Debt-related performance criteria.** The relevant performance criteria apply to the contracting and guaranteeing of new nonconcessional external debt by the government. The criteria apply to debt and commitments contracted or guaranteed for which value has not yet

¹ The following reference on the IMF website creates a link to a tool that allows for the calculation of the grant element of a broad range of financing packages: <http://www.imf.org/external/np/pdr/conc/calculator>.

² The calculation of concessionality will take into account all aspects of the debt agreement, including maturity, grace period, payment schedule, upfront commissions, and management fees.

³ For debts in foreign currencies for which the OECD does not calculate a CIRR, calculation of the grant element should be based on the composite CIRR (weighted average) of the currencies in the SDR basket.

been received. The criteria also apply to private debt for which official guarantees have been extended and which, therefore, constitute a contingent liability of the government. The performance criteria are measured on a cumulative basis from the time of approval of the ECF by the Executive Board. PCs will be monitored on a continuous basis. No adjuster will be applied to these criteria.

14. **Ceiling on short-term external debt newly contracted or guaranteed by the government.** Short-term external debt is external debt with the contractual term of less than one year. Debt-relief operations and treasury bills issued in CFA francs on the WAEMU regional market are excluded from this performance criterion. In the context of the program, the government and public enterprises will not contract, or guarantee, short-term external debt. This performance criterion is monitored on a continuous basis.

15. **Ceiling on new external payment arrears.** External payment arrears are defined as external payments due but not paid on the due date. In cases where a creditor has granted a grace period after the contractual due date, arrears are incurred following the expiration of the grace period. Under the program, the government undertakes not to accumulate arrears on its external debt, except those arising from government debt that is being renegotiated with creditors, including non-Paris Club bilateral creditors. This performance criterion is monitored on a continuous basis.

16. **Reporting requirements.** 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, but no later than within two weeks of such external debt being contracted or guaranteed.

17. **Social and other priority spending** is defined as total current expenditures in the education, health, and agricultural sector, and domestically financed capital spending (Table 4).

Table 4. Social and Priority Spending¹ by Quarter, 2011
(Cumulative, CFAF millions)

	March	June	Sept.	Dec.
	Prog.	Prog.	Prog.	Prog.
Social and other priority spending	2,932	5,864	8,795	12,227
Education	1,649	3,299	4,948	6,898
Health	897	1,794	2,691	3,788
Agriculture	264	527	791	1,055
Infrastructure	122	244	365	487

¹ Current and domestically financed capital spending.

B. Adjustors**18. The following adjustors will be in effect:**

- a. The ceiling on the domestic primary deficit (on a commitment basis) will be increased in case of lower than programmed disbursement of fishing compensation, by the amount of the shortfall up to a maximum of CFAF3 billion. The program assumes the following amounts of fishing compensation (cumulative from January 1, 2011): zero by end-March; zero by end-June; by end-September CFAF5 billion; and by end-December CFAF5 billion.⁴
- b. The ceiling on domestic financing will be increased for any shortfall in external budget support, and fishing compensation, by the amount of the shortfall up to a maximum of CFAF3.5 billion. The program assumes the following amounts of external budget support, and fishing compensation (cumulative from January 1, 2011): zero by end-March; zero by end-June; by end-September CFAF8.9 billion; and by end-December CFAF12.5 billion.
- c. The ceiling on domestic financing for March, June, and September will be increased for payment of previous years arrears in excess of programmed amounts up to a maximum of CFAF1.85 billion. The program assumes the following arrears payments from previous years (cumulative from January 1, 2011): zero by end-March; zero by end-June CFAF; zero by end-September; and by end-December CFAF1.85 billion.

⁴ For this TMU, the CFAF/euro exchange rate is 655.956 and the CFAF/US\$ exchange rate is 524.