International Monetary Fund

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

May 23, 2018

Letter of Intent

Kigali, Rwanda,
May 23, 2018

Ms. Christine Lagarde
Managing Director
International Monetary Fund
700 19th Street, N.W.
Washington, D.C., 20431

Dear Ms. Lagarde,

1. In the attached update of the Memorandum of Economic and Financial Policies (MEFP) and the Technical Memorandum of Understanding (TMU), we outline progress and policies toward meeting the objectives of the economic program of the Rwandan government that is supported by the PSI.

2. Following an adjustment program to deal with external shocks experienced in 2015 and a weather shock, growth slowed in 2016 and early 2017. However, because of dividends from our public investment strategies, increasing domestic production from our Made in Rwanda program, a more competitive real exchange rate, and favorable movements in international commodity prices, growth picked up in the second half of 2017, registering 6.1 percent for the year. The recovery was across most sectors of the economy, with a pronounced rebound in exports, reflecting strong performance in traditional exports combined with growing demand for new exports. Construction activity remained slack, however, following a boom in 2016 and possibly reflecting a lag in the response of domestic demand.

3. Fiscal policy has been in line with program objectives, and the debt situation remains at a low risk of distress. Monetary policy, following a period of modest easing in 2017, has been kept in a relatively neutral stance, as we transition toward implementation of an interest rate-based operating framework, in the context of a flexible exchange rate regime. All end-December 2017 and continuous quantitative assessment criteria under the program and structural benchmarks were met. The indicative US$500 million ceiling on new external debt contracted by public enterprises was exceeded by US$87 million, due to a lease signed by Rwandair. To accommodate this as well as other leases in the pipeline, we propose to raise the indicative ceiling to US$800 million.

4. Looking forward, we will continue to safeguard the progress made to sustain long-term economic growth, through keeping fiscal and external balances sustainable while implementing our new National Strategy for Transformation. Supporting reforms to our macroeconomic policies will

aim to improve domestic revenue mobilization, increase fiscal transparency, identify and mitigate potential fiscal risks.

5. In view of this performance, our Government requests that the Executive Board of the IMF approve the ninth review under the PSI-supported program. Proposed program targets for end-June 2018, which will gauge performance under the tenth and final review of the program, have been adjusted slightly to reflect more ambitious targets for accumulation of reserves, domestic revenues, and priority spending.

6. We are confident that the policies described in the attached MEFP will serve to achieve our program's objectives and, if necessary, our Government stands ready to take any additional measures that may be required. We will consult with the Fund on the adoption of such measures and in advance of revisions to the policies contained in the MEFP, in accordance with the Fund's policies on such consultation.

7. We consent to the publication of this letter, and its attachments as well as the related staff report.

Sincerely yours,

/s/	/s/
Uzziel Ndagijimana	**John Rwangombwa**
Minister of Finance and Economic Planning	Governor, National Bank of Rwanda

Attachments: I. Memorandum of Economic and Financial Policies
II. Technical Memorandum of Understanding

Memorandum of Economic and Financial Policies Kigali, Rwanda, May 23, 2018

I. INTRODUCTION

1. This MEFP reviews performance under the PSI-supported program through end-December 2017 and discusses the macroeconomic outlook and policies of the Government for 2018 and beyond. It also lays out proposed quantitative targets for end-June 2018 and structural benchmarks through December 1, 2018.

II. MACROECONOMIC DEVELOPMENTS AND PROGRAM PERFORMANCE THROUGH Q4 2017

Growth and Inflation.

2. In 2017, Rwanda rebounded from a slowdown in the first half of the year. The growth rate for the whole of 2017 was 6.1 percent against a projected 5.2 percent growth rate.

Main drivers of 2017 growth:

- Agriculture growth was 7 percent, thanks to a 7 percent growth in food crops, up from a 3 percent growth in 2016., Growth in industry was 4 percent compared to 7 percent in 2016, attributable to a decline in construction, which recorded growth of -3 percent in 2017. Mining sector growth boomed (21 percent) with the recovery in international prices and production of new minerals and gemstones while manufacturing growth remained at 6 percent, supported by food manufacturing and the growing textile sector. At 8 percent, the services sector also showed steady growth, with continued growth in tourism receipts as reflected in strong turnover growth in hotels and restaurants.
- Average annual headline inflation declined to 4.9 percent in 2017 from 5.7 percent in 2016. It eased to 2.8 percent in the second half of 2017 (2017H2) from 7.0 percent recorded in the first half of 2017 (2017H1). On a year-over-year basis, headline inflation continued to fall in March 2018 to 0.9 percent year on year, mainly due to negative food inflation. The evolution of food prices is largely explained by supplies; production was negatively affected in early 2017 by the 2016 drought but then improved over the course of 2017. To a lesser extent, inflationary pressure has also eased due to the stabilization of the RWF and the fading effects of a 2016 tariff increase,

Fiscal Performance and Financing

3. Budget execution in the first half of FY 2017/18 was broadly in line with expectations. Tax revenue collections marginally exceeded the target by 0.2 percent of GDP associated with improvements in corporate income taxes and VAT, and a large “one off” arrears collection. This over performance mitigated some shortfalls on excise taxes and taxes on international trade with

shortfalls on excise taxes explained by still-muted aggregate demand for highly-elastic consumer goods (beer, soft drinks, and cigarettes and mobile phone airtime). External disbursements of grants exceeded the projected amount by 0.3 percent of GDP due to the front loading of grants by a major donor.

4. On the spending side, total expenditure and net lending in the first half year of FY 2017/18 was about 0.2 percent of GDP higher than projected. With recurrent spending on track, the excess expenditure was caused by slightly higher capital expenditure resulting from accelerated construction of strategic petroleum reserve storage facilities and Global fund projects in health These expenditures were financed by drawdowns from accrued deposits of the strategic petroleum reserve levy introduced in fiscal year 2015/16 and accumulated deposits from Global Fund disbursements. The overall deficit (on a commitment basis) was 0.4 percent of GDP lower than expected.

Debt Management

5. Rwanda's risk of debt distress remains low. Rwanda has been able to maintain a low risk of debt distress through careful debt management and strong domestic revenue collection, combined with an improved macroeconomic environment. The Made in Rwanda policy strategy to stimulate domestic production, and the improvement in the country's trade balance have been key features in maintaining the low risk rating. Rwanda's debt sustainability analysis indicates a temporary breach of the debt service indicator thresholds, due to the 10-year Eurobond maturing in 2023.

6. Rwanda's debt stock stood at 47.1 percent of GDP at end-2017, a slight increase over 2016 attributable to budget support directed to for specific sectors (roads, energy and transport). Rwanda's external debt portfolio represented 78.6 percent of total public debt; 60 percent of the external debt portfolio consisted of concessional loans, which will continue to be the main source of funding for public projects. Domestic debt stood at 10.2 percent of GDP at end-2017. The government is extending the domestic debt maturity profile through more issuance of long-term bonds, as well the issuance of benchmark bonds (Bond re-opening) as an alternative to treasury bills. This will develop the bond market, reduce the number of outstanding series, and enhance liquidity in the market. In the first quarter of 2018, Rwandair contracted a lease for additional aircrafts for the expansion of its fleet, which breached the indicative target on the US$500 million ceiling on external debt by public enterprises US$87 million. The rationale behind fleet and route expansion is to operate deeper into Africa by adding new routes, and creating longer haul connections to Europe, America, and Asia. Although the initial plan was to acquire two aircraft next fiscal year, an opportunity arose to acquire new aircraft following the folding of a European airline company, so Rwandair management quickly engaged the lease contracts. The aircraft will only start generating debt service payments in 2019. Going forward, leases for 3 additional aircraft are likely to be signed in 2018, including to replace two aging aircraft. Hence, the government requests an increase in the indicative limit to US$800 million to accommodate these leases.

7. Going forward, Rwanda's debt management strategy will continue to focus on careful prioritization in project implementation. Appropriate financing models will be applied to avoid the

use of limited space for government borrowing in projects where the private sector could invest. The medium- term debt strategy will continue to focus on maximizing external concessional funding while promoting the domestic capital market.

Monetary Policy and Exchange Rate Developments.

8. The NBR's monetary policy stance remains broadly neutral. On 28th December 2017 the NBR's monetary policy committee (MPC) reduced the policy rate (KRR) from 6 percent to 5.5 percent based on current and expected developments in macroeconomic fundamentals, especially low inflation expectations, the relative stability of the RWF, and signs of still-weak aggregate demand.

9. The ease in exchange rate pressures in 2017 resulted from the improvement in Rwanda's export receipts in line with a continued recovery in international commodity prices, diversification of exports, and a decline in the import bill. The y/y RWF depreciation against the US$ moderated to 3.1 percent in 2017 from 9.7 percent in 2016.

10. Growth in monetary aggregates remains below historical trends on account of weak credit demand, but is rising associated with the improvement of activity in 2017: Private sector credit grew by 13.9 percent in 2017 compared to 9.1 percent in 2016

External Position

11. In 2017, the trade balance in merchandise improved substantially, driven by a strong 44.5 percent growth in exports and a 5.6 percent decline in imports. The strong performance in exports was driven by performance in all export categories, especially principal exports following the increase in international commodity prices, but also by exports in non-traditional categories such as other minerals and to a lesser extent horticulture. Other minerals include gemstones, tourmalines and amethyst and increased from 80 million USD in 2016 to 248 in 2017 while horticulture exports increased by 61 percent to 18.5 million USD.

12. Imports declined in 2017 partly due to the completion of some large construction projects such as the Kigali Convention Center and Marriot Hotel in the previous year which required the importation of big machines. The deceleration in some import subcategories, especially articles of clothing and construction materials, reflect investment policies to promote domestic production.

Financial Sector Stability

13. The pick-up of NPLs in the first half of the year 2017 reflects the subdued economic performance that affected the loan servicing capacity of borrowers. In line with the improved economic performance in the second half of 2017, NPLs dropped to 7.6 percent by end year from 8.2 percent recorded at mid-year.

14. *Banque Rwandaise de Developement* (*BRD*), a non-deposit taking development bank, was the only bank that did not comply with the minimum capital adequacy ratio of 15 percent at end December 2017. The bank is currently working at restructuring its balance sheet through a

conversion of Government special funds into capital in addition to a capital injection of RWF 15 billion already received from other shareholders. This restructuring is expected to bring the bank into compliance by year end.

15. The financial sector's legal and regulatory regime has evolved over the years to meet the changing structure of the Rwandan financial sector as well as related market developments. These prudential regulations relating to banking, microfinance institutions, non-banking financial businesses, and financial infrastructure aim to achieve a sound and efficient financial sector, benefitting depositors, stakeholders and other customers of financial institutions and the economy as a whole. The revised banking law gazetted in October 2017 offers the foundation for the financial sector to develop, comply with international best standards and, remain stable. The BNR is now in process of reviewing the banking regulations.

Program Performance.

16. All quantitative assessment criteria were met in the period under review, except the indicative ceiling on external borrowing for public enterprises, due to the aforementioned Rwandair leases. All structural benchmarks for the ninth review were met on time.

III. MACROECONOMIC OUTLOOK

Growth and Inflation.

17. In 2018, the overall GDP is projected to be 7.2 percent with an average in medium term of 7.7 percent, generally driven by agriculture and industry. Agricultural activity is projected to grow by 6 percent, due to projections for a strong main harvest. Industry is predicted to be the biggest contributor to overall GDP at 8.3 percent growth in 2018. This growth is expected to be led by a pick-up in construction activity, to 5.2 percent in 2018, following a contraction in 2017.

18. Mining sector growth is projected at 20.1 percent, and electricity is expected to grow at 11.9 percent due an increase in production capacity. Services growth is projected at 7.6 percent driven by trade and transport and supported by the good performance in agriculture and manufacturing.

19. Looking ahead, headline inflation is expected to remain around the 5.0 percent objective in 2018, as exchange rate pressures, global inflation, international commodity prices, and aggregate demand are foreseen to remain broadly subdued.

20. The main risk to the outlook remains weather conditions, which may affect the trend of food prices.

External Position

21. In 2018 and 2019, the current account is expected to deteriorate slightly to USD 867.2 and 1,026.9 million respectively due to higher imports from the construction of Bugesera airport. Exports

are expected improve in the medium term, while imports excluding Bugesera are expected to record a moderate increase as import substitution measures take effect. Despite the projected current account deterioration, higher financial flows in foreign direct investment and debt flows in 2018 and 2019 will boost the overall external position in the medium term, supporting a reserve build-up of 51.8 and 79.0 million in 2018 and 2019 respectively.

IV. PROGRAM POLICIES FOR 2018–19 AND THE MEDIUM TERM

22. Rwanda is developing its new long-term Vision 2050. The Vision 2050 emphasizes aspirations of high-quality livelihoods, and modern living standards for all Rwandan citizens. This prosperity will be achieved through increased incomes that require a long-term transformation of the economy with modern infrastructure and a sustainable environment at its core. The Rwandan Government recognizes that the country will need to transition from a foreign aid- and public investment -led growth model to one in which the private sector is in the lead role. In the longer run, the country needs to make decisive investments in future endowments: strengthening human capabilities, developing strong innovation capacity, and efficient forms of urbanization, and maintain effective and accountable institutions of governance. The Vision 2050 stipulates as pre-requisites, strong and sustainable macroeconomic fundamentals, including the need to sustain high private investment induced by domestic savings and capital inflows, high government investment, improved human capital through education and high productivity gains. The first years of Vision 2050 will be key to putting Rwanda on the trajectory for transformation. As such the first seven-year plan, the NST1, focuses on key priorities: creation of decent jobs, accelerating urbanization, establishing Rwanda as a knowledge based economy, shifting the exports base towards high value goods and services, increasing domestic savings and developing the financial services to promote private investment and increasing the productivity of agriculture. Rwanda will further invest in social protection and ensuring graduation from extreme poverty, in eradicating malnutrition and ensuring quality of education and health. Finally, social transformation is at the heart of national development and the Government will also emphasize capable and accountable institutions and ensuring continued citizens' participation and engagement in development, international development cooperation, security and safety, as well as justice, law and order.

A. Fiscal policy

Anticipated Outcomes for FY17/18.

23. The budget for fiscal year 2017/18 has been revised slightly to allow partial spending of higher than expected tax revenue collections. Accordingly, total tax revenue projection is being raised by around RWF 25 billion which represents 0.3 percent of GDP. Grants are expected to decline by 0.2 percent of GDP due to less RWF depreciation than originally forecast. As a result, total revenue and grants are now projected at 22.8 percent of GDP compared to 22.6 percent of GDP in PSI 8th review.

24. Consistent with the increase in revenue and grants, total expenditure and net lending were revised from PSI 8th review estimate but fell to 26.6 percent of GDP. This will allow the expenditure

of 0.2 percent of GDP to provide for the construction of schools and other infrastructure projects of the University of Rwanda, provision of health insurance for some citizens, insecticide spraying operations to reduce the spread of malaria, construction of irrigation systems to improve agricultural production, and pre- financing of some Peace Keeping Operations of the UN. The overall deficit is projected to decline to 3.8 percent of GDP compared to 4.2 percent of GDP in the revised budget. Reflecting the decline in overall deficit, the net domestic finance is also expected to decline.

Fiscal Policy Stance for the Medium-Term

25. Fiscal policy in the medium term will continue to reflect the policies of fiscal consolidation and prudent borrowing to keep debt and external balances sustainable. Consistent with these objectives, the overall deficit, is projected to decline to 4.2 percent of GDP in 2020/21. Tax revenue collections are projected to rise by 0.3 percent of GDP from FY2018/2019 to 16.2 percent in 2020/21. Increased yields from on-going tax policy and administrative measures mentioned above are expected to boost revenue collections in the medium term.

26. Implementation of expenditure prioritisation measures are expected to allow expenditures to decline from 26.9 percent of GDP in 2018/19 to 26.3 percent of GDP in 2020/21. The prioritisation strategy will mostly affect recurrent spending, which is projected to decline from 14.8 percent of GDP in 2018/19 to 13.9 percent in 2020/21.

27. Structural reforms for the coming year will focus on identifying fiscal risks and improving fiscal transparency (a FAD Fiscal Transparency Evaluation is expected to take place in H2 2018), maintaining the momentum for improving domestic revenue collection. At the same time, we are also making headway towards enhancing format, coverage, and timeliness of fiscal reporting via a transition to fiscal reporting according to the Government Finance Statistics Manual 2014 (GFSM 2014) and accrual accounting.

28. On public financial management, a fiscal risk analysis of hotel and insurance sectors to assess potential contingent liabilities has been initiated (structural benchmark). The objective of the analysis was to safeguard fiscal and financial sustainability. The assessment shows that, on a sample of 22 facilities representing 92 percent of total hotel NPLs, most hotel NPLs are in low and middle categories and only one in the upper risk category but it is not considered as ‘too big to fail’ and therefore does not pose any fiscal risks. The assessment of the insurance sector indicated an expectation of continued performance improvement for private insurers driven mainly by the recent review of tariffs for the motor business that was previously loss making as well as better conduct of business following the issuance of the Directive of Conduct of Insurance Business by the BNR. This directive is expected to curb previous malpractices such as price undercutting, issuing insurance on credit as well as fraud in claims settlement. Solvency of private insurers improved from 78 percent in December 2016 to 193 percent in December 2017 and is expected to close 2018 above the minimum 100 percent. NBR will continue to monitor these two sectors closely to mitigate any potential costs to the budget or debt implication.

29. **Key Policy objectives in 2018/19 and over the medium term** are guided by NST1 interventions in the area of; (i) *Jobs creation* through NEP Interventions in various sectors with focus on youth and women including and Hands-on skills development through TVET and accessing start up toolkits; (ii) *Urbanization*; with the implementation of City of Kigali & Secondary City Master Plans and improvement of rural and urban transportation services; (iii) *Competitive Knowledge-Based Economy*; Operationalization of the Rwanda Innovation fund and the support to centres of Excellence; (iv) *Industrialization and Export Promotion*; Development of industrial parks, Kigali Logistic Platform, and Bonded warehouse at the borders and Exploration of Mineral Potentials. We will also continue to implement our strategy for Tourism diversification; continuing construction of Bugesera Airport, support to Rwandair expansion, development of new tourism products, etc.); (v) *Increasing Agriculture & Livestock Production and Productivity and Establishing Agriculture financing and insurance scheme*; (vi) *Sustainable Management of Natural Resources and Environment*; (vi) *Domestic Savings Promotion* through subscription to Long Term Saving Scheme, implementation of the 10-Year Capital Market Master Plan, Operationalization of the World-Class Payment Eco-system to promote Rwanda into a cashless Economy etc.

30. The 2018/19 budget will continue to reflect the policies of prudent spending and borrowing to keep debt and external balances sustainable. The fiscal deficit, excluding peacekeeping operations, is expected to rise slightly from 2.5 percent of GDP in 2017/18 to 3.1 percent of GDP in 2018/19 and thereafter remain at this level in 2019/20 and 2020/21. (Including peacekeeping operations, due to mismatches between spending and repayment, the deficit is projected to rise slightly from 3.8 percent of GDP in 2017/18 to 4.6 percent of GDP in 2018/19.)

31. Correcting for one-off arrears collection in FY17/18, tax revenue collections are projected to remain flat, at 15.6 percent of GDP. in 2018/19.

32. **Tax policy changes** involving the 'EBM for all' which aims at rolling out the EBMs to selected non-VAT registered tax payers, enactment of the law amending excise duties on beer, wines and liquors as well as mobile data and amendments to taxes on income involving capping of management fees to 2 percent, excluding liberal professionals from the lump-sum/flat regime and the implementation of the transfer pricing guidelines which will help the Rwanda Revenue Authority conduct proper audits of multilateral companies (banks, telecoms, insurance and mining companies etc.) are expected to boost revenue collections in 2018/19 and help achieve the tax revenue target for FY2019/20 as some of the policy changes will take effect with a lag.

33. Total expenditure and net lending in 2018/19 are projected to rise marginally to 26.8 percent of GDP from 26.6 percent of GDP in 2017/18. Recurrent spending is being increased by 0.3 percent of GDP to account for the on-going restructuring of Government machinery, inclusion of expenditures to be funded with internally generated funds of some public institutions, and increased spending on Peacekeeping Operations.

34. In the case of capital spending, priority for funding allocation goes to the completion of on-going projects that promote growth. Foreign investment spending is increased by 0.3 percent of

GDP as a result of increased capital grants disbursement, reflecting improved performance partly attributable to the uptake of the e-procurement system.

35. The overall deficit in 2018/19 is projected at 4. 6 percent of GDP as against 3.8 percent of GDP in 2017/18. Net domestic finance will amount to 0.6 percent of GDP in 2018/19.

B. Monetary Policy

36. In the context of subdued inflation and exchange rate pressures, monetary policy will remain supportive to help bolster improving, but still below potential, aggregate demand. The growing instability of the money multiplier has exacerbated the disconnection between reserve money and broad money, posing challenges to the monetary targeting framework under which the NBR conducts its monetary policy. In this regard, the NBR is shifting to a price-based monetary policy framework to further improve the effectiveness of monetary policy.

37. In Rwanda, price-based monetary policy implementation would make money market rates more stable and predictable, a condition conducive to developing financial markets further and strengthening the monetary transmission mechanism. The NBR undertook steps to implement preconditions to move to an interest-based monetary policy framework, especially those related to management of liquidity and policymaking processes.

- **Interbank market development**. A well-functioning interbank market not only facilitates liquidity management by banks, but also serves as the cornerstone of financial market development. Similarly, through active and consistent management of system liquidity, the NBR can influence the determination of interest rate in the interbank money market. In this context, the NBR will soon launch an electronic interbank trading platform to enhance information sharing among market participants and improve price discovery (structural benchmark).
- **Communication**. When central banks make the transition from quantitative to market based monetary policy, effective communication is imperative. In this regard, the NBR is developing a strong communication strategy that will enhance its transparency and accountability. It will aim to effectively communicate its policy decisions, economic developments and outlook, and strengthen the communications content of the inflation report to better anchor price expectations. This will be important for markets and the public to understand the nature of shocks and NBR's policy responses. In this respect, the program contains structural benchmarks about establishing optimal inflation ranges and developing a strategy for improving communications.
- **Capacity development**. The NBR is seeking technical assistance to help build in-house capacity and identify constraints in the transition.
- **Forecasting and policy analysis system (FPAS).** The NBR has developed a forecasting and policy analysis system (FPAS), with the help of technical assistance by the IMF. Publications have been restructured to become more compatible with forward-looking communication, in particular, creating a more forward-looking inflation report. The NBR will continue to

operationalize the FPAS, by formalizing the forecasting team and process and integrating it further into monetary policy decision-making.

- **Determine the optimal level of inflation range**. Having committed to move towards a price-based monetary policy framework, the NBR is conducting a study which will recommend an optimal band for headline or core inflation.
- **Reduce the level of excess reserves.** Rwanda's banking system faces persistent and volatile excess in bank reserves, which pose a challenge to monetary policy transmission. In this regard, the NBR made progress and the "Financial Market Operations Committee" in charge of daily financial market analysis, liquidity management and forecasting continued to be strengthened. The NBR continued regular discussions initiated in 2017 with commercial bank treasurers about market developments and analysis. As result, the interbank market activity has continued to grow in both depth and width, and the NBR has succeeded in keeping the interbank market rate close to the Key Repo Rate for almost two consecutive years. These good developments are expected to continue in 2018 and beyond.

38. NBR is also taking steps to deepen the government securities market and enhance the yield curve. These include establishing a re-opening mechanism for long-term bonds (reissuing the same bond on different occasions), which would gradually build their outstanding volumes to the desired levels to qualify them as benchmark bonds. During the fiscal year 2017-2018, NBR (on behalf of Government of Rwanda) issued a 5-year bond in August 2017 and February 2018; a 7-year bond in November 2017 and is planning to issue a 10-year bond at end May 2018. On 28th March 2018, NBR issued a directive related to the regulatory framework for Government Bonds which included a discussion of the Reopening mechanism (Structural benchmark). The mechanism will be implemented by end June 2018 with a planned reopening of a 7-year bond issued in 2016.

Table 1. Status of Structural Benchmarks under the PSI-Supported Program	
Policy Measure	**Target Date**
Monetary	
Establish an optimal level of headline or core inflation target range for monetary policy	10th PSI Review
Develop and adopt a communication strategy on the objectives and operations of the monetary policy framework to enhance BNR transparency and accountability	10th PSI Review
Financial Market	
Introduce Government bond reopening mechanisms with objective to develop benchmark bonds and promote depth and liquidity in the government bond market.	Met
Establish an electronic interbank trading platform intended to improve banks' counterparty visibility and price formation in the market.	10th PSI Review
Public Financial Management	
Provide quarterly revenues, expenditures, and financing estimates for the budgetary central government levels within 60 days of the end of each quarter.	Met
Begin publishing in GFS 2014 format for the quarter ending September 2018.	10th PSI Review
Initiate a fiscal risk analysis of hotel and insurance sectors to assess potential contingent liabilities.	Met
Fiscal Revenues	
Initiate the rollout of "EBM version 2" pilot, with the intent of reaching 1,000 new EBM users.	10th PSI Review

Table 2. Quantitative Assessment Criteria and Indicative Targets

	December 2017				June 2018
	Program	Adjusted	Actual	Status	Proposed Program
(Billions of Rwandan francs, unless otherwise indicated)					
Assessment criteria					
Ceiling on the overall fiscal deficit, including grants[2, 3]	241	251	168	Met	325
Net foreign assets of the NBR at program exchange rate (floor on stock)[3]	657		736	Met	628
Reserve money (ceiling on stock) (upper bound)[4]	348		313		365
Reserve money (stock)[4]	341			Met	357
Reserve money (ceiling on stock) (lower bound)[4]	333				349
External payment arrears (US$ millions) (ceiling on stock)[5]	0			Met	0
Indicative targets					
Net domestic financing (ceiling on flow)[2, 3]	-35	-11	-76	Met	7
Domestic revenue collection (floor on flow)[2, 6]	556		613	Met	1300
Net accumulation of domestic arrears (ceiling on flow)[2]	0		-4	Met	0
Total priority spending (floor on flow)[2]	346		349	Met	745
New external debt contracted or guaranteed by nonfinancial public enterprises (US$ millions) (ceiling on stock)[5]	500		634	Not met	800
Memorandum items:					
Total budget support (US$ millions) [2, 6]	331		314		161
Budget support grants (US$ millions)	101		129		87
Budget support loans (US$ millions)	230		185		73
RWF/US$ program exchange rate	830		830		845

Sources: Rwandan authorities and IMF staff estimates and projections.

1 All items including adjusters are defined in the Technical Memorandum of Understanding (TMU).

2 Numbers for December 2017 and June 2018 are cummulative from 6/30/2017.

3 Subject to adjustors. See TMU for details.

4 Targets are calculated as an arithmetic average of the stock of reserve money for the 3 months in the quarter. AC and PC applies to upper bound only.

5 Ceilings on external arrears and external borrowing are continuous. The ceiling will exclude onlending agreement between Government of Rwanda and public sector enterprises.

6 Excluding demobilization and African Union peace keeping operations, HIPC and COMESA grants.

Technical Memorandum of Understanding

Kigali, Rwanda, May 23, 2018

1. This memorandum defines the quantitative targets described in the memorandum of economic and financial policies (MEFP) for the period July 1**,** 2017–December 1, 2018 supported by the IMF Policy Support Instrument (PSI), and sets out the data reporting requirements. This TMU updates the one of July 12, 2017.

I. QUANTITATIVE PROGRAM TARGETS

2. The quantitative program will be assessed through assessment criteria (QAC) and indicative targets (IT) for the duration of the program.

3. QACs will apply for the following indicators for December 31, 2017 and June 30, 2018 (the test dates) throughout the program period:

- Floor on stock of net foreign assets (NFA) of the National Bank of Rwanda (NBR);
- Ceiling on stock of reserve money;
- Ceiling on the overall fiscal deficit, including grants as measured on a commitment basis; and
- Ceiling on stock of external payment arrears of the public sector (assessed on a continuous basis throughout the program period).

4. IT will apply to the following indicators for December 31, 2017 and June 30, 2018 (the test dates) throughout the program period:

- Ceiling on flow of net domestic financing (NDF) of the budgetary central government;
- Floor on flow of domestic revenue collection of the budgetary central government;
- Ceiling on flow of net accumulation of domestic arrears of the budgetary central government;
- Ceiling on contracting or guaranteeing of new non-concessional external debt of nonfinancial public enterprises (assessed a continuous basis throughout the program period); and
- Floor on flow of priority spending.

5. Program exchange rates. For accounting purposes, the program exchange rates in Text Table 1 will apply.

Text Table 1. Program Exchange Rates from January 1, 2018 (US$ per currency unit, unless indicated otherwise)	
Rwanda Franc (per US$)	845.00
Euro	1.20
British Pound	1.35
Japanese Yen (per US$)	112.90
SDR	1.42

II. INSTITUTIONAL COVERAGE OF THE FISCAL SECTOR

6. The budgetary central government fiscal operation table comprises the treasury and line ministries, hereafter referred to as "the government" unless specified otherwise.

III. TARGETS RELATED TO THE EXECUTION OF THE FISCAL PROGRAM

Ceiling on Net Domestic Financing of the Government (IT)

7. A ceiling applies to NDF. The ceilings for December 31, 2017, and June 30, 2018, are cumulatively measured from June 30, 2017.

8. Definition. NDF of the government is defined as the change in the sum of (i) net banking sector credit to the government and (ii) non-bank holdings of government domestically issued debt.

9. Net banking sector credit to the government is defined as

- Consolidated credit to the government from the banking system (NBR and commercial banks, as recorded in the monetary survey). The outstanding consolidated government debt held by the banking system,1 includes government debt to the NBR amounting to RWF 38.6 billion incurred as a result the overdraft to the pre-war government and the 1995 devaluation2, as well as the current overdraft with the NBR. Credit to the government will exclude treasury bills issued by the NBR for monetary policy purposes, the proceeds of which are sterilized in deposits held as other NBR liabilities.
- Less total government deposits with the banking system (as recorded in the monetary survey), including in the main treasury account, the accounts of line ministries, the fund for assistance to genocide survivors, the Rwanda Revenue Authority, the electoral commission, the demobilization commission, fonds routier, the privatization account, and the accounts of any other autonomous public enterprises and public agencies over which the government has direct control over their deposits. Thus, this definition excludes any government deposits over which the budgetary central government does not have any direct control (i.e., for project

[1] Consisting of bank holdings of treasury bills, bonds (domestic), old development bonds (pre-1994 debt), new development bonds (including those used for recapitalization of banks), and other accounts receivable.

[2] The authorities will inform Fund staff of any substantive changes in government accounts with the banking system, which may affect the calculation of net bank claims.

accounts, Global Fund money meant for the private sector, counterpart funds, and fonds publics affectés.)

10. Non-bank holdings of government domestically issued debt consist of non-bank holdings of treasury bills, bonds (domestic and non-resident), old development bonds (pre-1994 debt), new development bonds (including those used for recapitalization of banks), and other accounts receivable.

Adjusters to NDF:

- The ceiling on NDF will be adjusted upward by the amount of any shortfall between actual and programmed budgetary grants and loans (as defined in Table 1 of the MEFP), up to a maximum of RWF 78billion. In the event that actual budgetary grants exceed programmed levels, the ceiling on NDF will not be adjusted. In the event that actual budgetary loans exceed programmed levels, the ceiling on NDF will be adjusted downward.
- The ceiling on NDF will be adjusted upward up to a maximum of RWF 78 billion representing the amount of foreign financed capital expenditure financed with draw-down of accumulated government deposits as specified in the definition of NDF.
- The ceiling on NDF will be adjusted upward by the amount of unexpected public expenditures on food imports in the case of a food emergency.
- The ceiling on NDF will be adjusted upward (downward)up to a maximum of RWF 78 billion, by any unplanned financing shortfall (surplus) from Peace Keeping Operations.

Overall Fiscal Deficit Including Grants (QAC)

11. A ceiling applies to the overall fiscal deficit including grants. The ceilings for December 31, 2017, and June 30, 2018, are cumulatively measured from June 30, 2017.

12. Definition. For the program, the overall fiscal deficit including grants is valued on a commitment basis. That is, the overall fiscal balance is the difference between the government's total revenue and grants and total expenditure and net lending (costs and acquisition net of nonfinancial assets). Government expenditure is defined on the basis of payment orders accepted by the Treasury, as well as those executed with external resources. This assessment criterion is set as a floor on the overall fiscal deficit as of the beginning of the year.

Adjusters to the Overall Fiscal Deficit Including Grants:

- The ceiling on the overall deficit will be adjusted upward by the amount of any shortfall between actual and programmed budgetary grants (as defined in Table 1 of the MEFP), up to a maximum of RWF 78 billion.
- The ceiling on the overall deficit will be adjusted upward, up to a maximum of RWF78 billion, representing the amount of foreign financed capital expenditure financed with draw-down of accumulated government deposits as specified in the definition of NDF.

- The ceiling on the overall deficit will be adjusted upward by the amount of unexpected public expenditures on food imports in the case of a food emergency.
- The ceiling on the overall deficit will be adjusted upward (downward), up to a maximum of RWF78 billion, by any unplanned financing shortfall (surplus) from Peace Keeping Operations.

Floor on Flow of Domestic Revenues (IT)

13. The floors for December 31, 2017, and June 30, 2018, are cumulatively measured from June 30, 2017.

14. Definition. The floor on domestic government revenue is defined as total government revenue (tax and non-tax revenues), per the budgetary central government statement of operations table, but including: (a) local government taxes (comprised of business licenses, property tax, and rental income tax); and (b) local government fees; and excluding and receipts from Peace Keeping Operations.

Floor on Priority Expenditure

15. The floor applies to priority spending of the government. The floors for December 31, 2017, and June 30, 2018, are cumulatively measured from June 30, 2017.

16. Definition. Priority expenditure is defined as the sum of those recurrent expenditures, domestically-financed capital expenditures, and net lending that the government has identified as priority in line with the EDPRS2/NTS. Priority expenditure is monitored through the Integrated Financial Management System (IFMS) which tracks priority spending of the annual budget at the program level.

Net Accumulation of Domestic Expenditure Arrears of the Government (IT)

17. A ceiling applies to net accumulation of domestic expenditure arrears of the government.[3] The ceilings for December 31, 2017, and June 30, 2018, are cumulatively measured from June 30, 2017.

18. Definition. Domestic expenditure arrears are defined as unpaid claims that are overdue by more than 90 days. These will include payments for tax refunds, employee expenses (wages and salaries, staff claims for travel, and other non-salary allowances), utilities, rents, recurrent goods and services, and construction works. Accumulation of domestic expenditure arrears of more than 90 days is calculated as a cumulative change in the stock of expenditure arrears of more than 90 days at each test date from the stock at the end of the previous fiscal year (June 30). Arrears related to claims preceding 1994 will not be counted in the calculation.

[3] A negative target thus represents a floor on net repayment.

IV. LIMITS ON DEBT

Limit on New External Debt of Nonfinancial Public Enterprises (IT)

19. A ceiling applies to the contracting and guaranteeing by nonfinancial public enterprises of new external borrowing with non-residents (see below for the definition of debt guarantee and debt). The ceiling excludes external borrowing by two state-owned banks, the Bank of Kigali and Rwanda Development Bank (BRD), which are assumed not to seek or be granted a government guarantee. The ceiling also applies to private debt for which official guarantees have been extended, including future swaps involving foreign currency loans guaranteed by the public sector (see below for swaps), and which, therefore, constitute a contingent liability of the public sector. The ceiling will exclude external borrowing which is for the sole purpose of refinancing existing public-sector debt and which helps to improve the profile of public sector debt. The ceiling will also exclude on-lending agreement between Government of Rwanda and public-sector enterprises.

20. Public sector includes the government, entities that are part of the budgetary process and nonfinancial public enterprises which are entities in which the government holds a controlling stake (owning more than 50 percent of shares), but which are not consolidated in the budget. This definition of the public sector excludes and Rwanda Development Bank (BRD). For program purposes, the guarantee of a debt arises from any *explicit* legal obligation of the public sector to service a debt in the event of nonpayment by the debtor (involving payments in cash or in kind).

21. The definition of debt is set out in paragraph 8(a) of the Guidelines on Public Debt Conditionality in Fund Arrangements attached to Executive Board Decision No. 15688-(14/107), adopted December 5, 2014.

(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 lesser retains the title to the property. The debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property.

(b) Under the definition of debt set out in this paragraph, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes 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.

Limit on the Stock of External Payment Arrears

22. A continuous performance/assessment criterion applies to the non-accumulation of payment arrears on external debt contracted or guaranteed by the government and entities that form part of the budgetary process. External payment arrears consist of external debt service obligations (principal and interest) that have not been paid at the time they are due, as specified in the contractual agreements, but shall exclude arrears on obligations that are subject to rescheduling. For the purpose of monitoring compliance with the PC on the non-accumulation of external arrears, external arrears are obligations that have not been paid on the due date (taking into account the contractual grace periods, if any). External payments arrears on external debt service obligations by nonfinancial public enterprises that the government holds a controlling stake (owning more than 50 percent of shares) but do not form part of the budgetary process and public private partnership projects (which are defined as: (i) infrastructure projects which involve the, (ii) granting of a government guarantee, and the (iii) participation of a public enterprise) are not included in the coverage of this external arrears PC/AC, unless these external payment arrears are overdue (under the terms of the contracts including any grace periods) by more than 30 days.

V. TARGETS FOR MONETARY AGGREGATES

Net Foreign Assets of the National Bank of Rwanda (QAC)

23. A floor applies to the net foreign assets (NFA) of the NBR for December 31, 2017 and June 30, 2018.

24. **Definition.** NFA of the NBR in Rwandan francs is defined, consistent with the definition of the Special Data Dissemination Standard (SDDS) template, as external assets readily available to, or controlled by, the NBR net of its external liabilities. Pledged or otherwise encumbered reserve assets (including swaps) are excluded; such assets include, but are not limited to, reserve assets used as collateral or guarantee for third party external liabilities. Reserves assets corresponding to undisbursed project accounts are also considered encumbered assets and are excluded from the measurement of NFA for program purposes. Foreign assets and foreign liabilities in U.S. dollars are converted to Rwandan francs by using the U.S. dollar/Rwanda franc program exchange rate. Foreign assets and liabilities in other currencies are converted to U.S. dollars by using the actual end-of-period U.S. dollar/currency exchange rate. Foreign liabilities include, inter alia, use of IMF resources.

Adjusters:

- The floor on NFA will be adjusted downward by the amount of any shortfall between actual and programmed budgetary loans and grants per Table 1 of the MEFP, capped at RWF 78 billion.
- The floor on NFA will be adjusted downward (upward) by the surplus (shortfall) of cash external debt service payments compared to originally-scheduled payments.
- The floor on NFA will be adjusted downward by the amount of unexpected public expenditures on food imports in the case of a food emergency.

Reserve Money (QAC)

25. A ceiling applies to the stock of reserve money for December 31, 2017 and June 30, 2018 as indicated in Table 1. Quantitative Assessment Criteria and Indicative Targets of the MEFP. The ceiling is the upper bound of a reserve money band (set at+/- 2.2 percent) around a central reserve money target).

26. The stock of reserve money for a given quarter will be calculated as the arithmetic average of the stock of reserve money at the end of each calendar month in the quarter. Daily average of all the three months in the quarter will constitute the actual reserve money to be compared with the target.

27. **Reserve money** is defined as the sum of currency in circulation, commercial banks' reserves, and other nonbank deposits at the NBR.

Adjuster:

- The ceiling on the stock of reserve money will be adjusted symmetrically for a change in the required reserve ratio of commercial banks. The adjustor will be calculated as (new reserve ratio minus program baseline reserve ratio) multiplied by actual amount of liabilities (Rwanda Franc plus foreign-currency denominated) in commercial banks.

VI. DATA REPORTING REQUIREMENTS

28. For the purposes of program monitoring, the Government of Rwanda will provide the data listed below and in Table 1. Unless specified otherwise, weekly data will be provided within seven days of the end of each week; monthly data within five weeks of the end of each month; quarterly data within eight weeks of the end of each quarter; annual data as available.

29. Data on **NDF** (showing separately treasury bills and government bonds outstanding, other government debt, and budgetary central government deposits), each type of debt to be shown by debt holder, will be transmitted on a monthly basis. Deposits of the government with the NBR and with the commercial banks will be separated from the deposits of the public enterprises and autonomous public agencies and agencies that the government does not have any direct control over.

30. Detailed data on **domestic revenues** will be transmitted on a monthly basis. Data on **priority expenditure** will be transmitted on a quarterly basis. Data on accumulation and repayment of **domestic arrears** and the remaining previous year's stock of arrears will be transmitted on a quarterly basis.

31. Data on **foreign assets and foreign liabilities of the NBR** will be transmitted on a weekly basis, including breakdown of assets that are pledged or encumbered. This transmission will include daily and weekly data on the NBR's foreign exchange liabilities to commercial banks (including required reserves with the NBR) and the exchange rate used for their conversion into Rwanda francs will be shown separately.

32. Data on **reserve money** will be transmitted on a weekly basis. This transmission will include a daily and a weekly balance sheet of the NBR which will show all items listed above in the definitions of reserve money

33. The authorities will inform the IMF staff in writing prior to making any changes in economic and financial policies that could affect the outcome of the financial program. Such policies include, but are not limited to, customs and tax laws, wage policy, and financial support to public and private enterprises. The authorities will inform the IMF staff of changes affecting respect of continuous QACs and ITs. The authorities will furnish a description of program performance according to QACs and ITs as well as structural benchmarks within 8 weeks of a test date. The authorities engage to submit information to IMF staff with the frequency and submission time lag indicated in TMU Table 1. The information should be mailed electronically to the Fund. (email: afrrwa@imf.org).

TMU Table 1. Summary of Reporting Requirements			
	Frequency of Data[9]	Frequency of Reporting[9]	Frequency of Publication[9]
Exchange Rates[1]	D	W	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[2]	W	W	M
Reserve/Base Money	W	W	M
Broad Money	M	M	M
Central Bank Balance Sheet	W	W	M
Consolidated Balance Sheet of the Banking System	M	M	M
Interest Rates[3]	M	M	M
Volume of transactions in the interbank money market and foreign exchange markets and sales of foreign currencies by NBR to commercial banks	D	W	W
Consumer Price Index[4]	M	M	M
Composite Index of Economic Activity (CIEA) and sub-components compiled by the NBR	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[5] – General Government[6]	A	A	A
Revenue, Expenditure, Balance and Composition of Financing[5]– Budgetary Central Government	Q	Q	Q
Financial balance sheet – Budgetary Central Government	A	A	A
Comprehensive list of tax and other revenues[7]	M	M	M
Comprehensive list of domestic arrears of the government	SA	SA	SA
Stocks of public sector and public-Guaranteed Debt as compiled by MINECOFIN and NBR[8]	Q	Q	Q
External Current Account Balance	A	SA	A
Exports and Imports of Goods and subcomponents.	M	M	Q
Exports and Imports of Goods and Services and subcomponents	A	A	A
GDP/GNP	A, Q	Q, SA	Q

[1] Includes the official rate; Foreign Exchange Bureau Associations rate; weighted average of the interbank money market rates; and weighted average of the intervention rate by the NBR.
[2] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[3] Both market-based and officially-determined, including discount rates, money market rates, interbank money market rate, rates on treasury bills, notes and bonds.
[4] Includes General Index; Local Goods Index; Imported Goods Index; Fresh Products Index; Energy Index; General Index excluding Fresh Products and Energy; and their breakdowns as published by the NISR.
[5] Foreign, domestic bank, and domestic nonbank financing.
[6] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[7] Includes proceeds from privatization, accompanied by information on entities privatized, date of privatization, numbers and prices of equities sold to the private sector.
[8] Includes debts of the Bank of Kigali. Also includes currency and maturity composition.
[9] Daily (D); Weekly (W); Monthly (M); Quarterly (Q); Annually (A); Semi-annually (SA); Irregular (I).